

SYNCORA HOLDINGS LTD.

Consolidated Financial Statements

**As of March 31, 2019 (Unaudited) and December 31, 2018 and for the
Three Months Ended March 31, 2019 and 2018 (Unaudited)**

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SYNCORA HOLDINGS LTD.
CONSOLIDATED BALANCE SHEETS
MARCH 31, 2019 (Unaudited) and DECEMBER 31, 2018
(U.S. dollars in thousands, except share and per share amounts)

ASSETS	2019	2018
Cash and invested assets:		
Debt securities, available-for-sale, at fair value (amortized cost: \$617,505 and \$613,167).....	\$ 627,755	\$ 613,488
Other invested assets, at fair value (cost: \$91,502 and \$91,364).....	94,641	87,504
Cash and cash equivalents.....	65,557	150,388
Total cash and invested assets.....	787,953	851,380
Insurance operating assets, retained business:		
Premiums receivable.....	14,425	14,260
Salvage and subrogation recoverable.....	168,724	147,866
Receivables on insurance cash flow certificates, net of deferred gains of \$112,751 and \$113,433.....	77,954	91,905
Deferred acquisition costs and deferred loss on reinsurance, net.....	17,890	18,423
Assets of consolidated variable interest entities, at fair value.....	19,407	20,843
Total insurance operating assets, retained business.....	298,400	293,297
Insurance operating assets, ceded business:		
Premiums receivable.....	42,526	42,458
Prepaid reinsurance premiums.....	108,593	112,011
Reinsurance recoverable on unpaid losses and loss adjustment expenses.....	116,689	120,011
Credit default and other swap contracts, at fair value.....	226,204	227,052
Total insurance operating assets, ceded business.....	494,012	501,532
Other assets.....	52,554	44,173
Total assets.....	\$ 1,632,919	\$ 1,690,382

LIABILITIES AND SHAREHOLDERS' EQUITY

Insurance operating liabilities, retained business:		
Unpaid losses and loss adjustment expenses.....	\$ 312,508	\$ 365,774
Unearned premium revenue.....	27,714	28,500
Credit default and other swap contracts, at fair value.....	10,849	8,489
Liabilities of consolidated variable interest entities, at fair value.....	316	340
Total insurance operating liabilities, retained business.....	351,387	403,103
Insurance operating liabilities, ceded business:		
Reinsurance premiums payable.....	42,526	42,458
Unearned premium revenue.....	108,593	112,011
Unpaid losses and loss adjustment expenses.....	116,689	120,011
Credit default and other swap contracts, at fair value.....	226,204	227,052
Total insurance operating liabilities, ceded business.....	494,012	501,532
Notes payable (par value: \$150,137 and \$150,137).....	107,441	104,206
Accrued interest on notes payable.....	18,965	16,472
Other liabilities.....	13,339	15,545
Total liabilities.....	985,144	1,040,858

Shareholders' equity

Non-controlling interest in subsidiary- Series B perpetual non-cumulative preferred shares of Syncora Guarantee Inc. (2,000 shares authorized and issued; 581 and 1,345 shares outstanding, 1,419 and 655 shares held by subsidiary; \$58,126 and \$134,526 liquidation preference).....	5,813	13,453
Non-controlling interest in consolidated entity.....	1,861	2,247
Common shares (500,000,000 shares authorized; 90,102,159 and 90,013,135 shares issued; 87,057,571 and 86,968,547 shares outstanding, 3,044,588 shares held as treasury; \$0.01 par value) and additional paid-in capital.....	2,718,162	2,717,633
Accumulated deficit.....	(2,089,896)	(2,085,637)
Accumulated other comprehensive income.....	11,835	1,828
Total Syncora Holdings Ltd. shareholders' equity.....	640,101	633,824
Total shareholders' equity.....	647,775	649,524
Total liabilities and shareholders' equity.....	\$ 1,632,919	\$ 1,690,382

See accompanying Notes to Unaudited Consolidated Financial Statements.

SYNCORA HOLDINGS LTD.
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS) (Unaudited)
THREE MONTHS ENDED MARCH 31, 2019 AND 2018
(U.S. dollars in thousands, except share and per share amounts)

	<u>2019</u>	<u>2018</u>
Revenues		
Premiums earned, net of reinsurance ceded of \$3,686 and \$1,588.....	\$ 635	\$ 14,303
Net investment income.....	8,589	10,381
Net unrealized and realized gains on investments, including other-than-temporary impairment losses of \$(449) and \$(10,885).....	6,681	996
Net (loss) earnings on insurance cash flow certificates.....	(13,728)	34,333
Net loss on credit default and other swap contracts.....	(1,878)	(21,104)
Net change in fair value of consolidated variable interest entities.....	290	1,870
Other income and fees.....	1,227	16,205
Total revenues	<u>1,816</u>	<u>56,984</u>
Expenses		
(Recoveries) losses and loss adjustment expenses, net of reinsurance ceded of \$(623) and zero.....	(71,814)	35,317
Amortization of deferred acquisition costs, including deferred loss on reinsurance.....	533	2,314
Interest expense, including accretion of \$3,235 and \$12,425.....	5,728	24,473
Operating expenses.....	13,890	10,419
Total expenses	<u>(51,663)</u>	<u>72,523</u>
Income (loss) before income tax expense from continuing operations	53,479	(15,539)
Income tax expense.....	483	-
Income (loss) from continuing operations	52,996	(15,539)
Income from discontinued operations, net of tax	-	6,866
Net income (loss)	<u>52,996</u>	<u>(8,673)</u>
Other comprehensive income (loss):		
Other comprehensive income (loss) from continuing operations.....	10,007	(13,068)
Other comprehensive loss from discontinued operations.....	-	(3)
Other comprehensive income (loss)	<u>10,007</u>	<u>(13,071)</u>
Comprehensive income (loss)	<u>\$ 63,003</u>	<u>\$ (21,744)</u>
Net (loss) income and comprehensive (loss) income attributable to non-controlling interest	<u>\$ (45)</u>	<u>\$ 104</u>
Net income (loss) and comprehensive income (loss) attributable to controlling interest:		
Net income (loss).....	\$ 53,041	\$ (8,777)
Comprehensive income (loss).....	\$ 63,048	\$ (21,848)
Calculation of basic and diluted earnings (loss) per share attributable to Syncora Holdings Ltd. common shareholders:		
Income (loss) from continuing operations.....	\$ 53,041	\$ (15,643)
Accounting effect of the purchase of Series B perpetual non-cumulative preference shares.....	<u>(57,300)</u>	<u>-</u>
Total.....	(4,259)	(15,643)
<i>Per share</i>	\$ (0.05)	\$ (0.18)
Income from discontinued operations.....	\$ -	\$ 6,866
<i>Per share</i>	\$ -	\$ 0.08
Loss.....	\$ (4,259)	\$ (8,777)
<i>Per share</i>	\$ (0.05)	\$ (0.10)
Weighted average common shares outstanding.....	87,012,070	86,836,445

See accompanying Notes to Unaudited Consolidated Financial Statements.

SYNCORA HOLDINGS LTD.
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY (Unaudited)
THREE MONTHS ENDED MARCH 31, 2019 AND 2018
(U.S. dollars in thousands, except share amounts)

	<u>2019</u>	<u>2018</u>
Non-controlling interest in subsidiary – Series B perpetual non-cumulative preferred shares of Syncora Guarantee Inc.		
Balance—beginning of period.....	\$ 13,453	\$ 13,453
Carrying value reduction related to the purchase of Series B perpetual non-cumulative preference shares.....	<u>(7,640)</u>	<u>-</u>
Balance—end of period.....	<u>5,813</u>	<u>13,453</u>
Non-controlling interest in consolidated entity		
Balance—beginning of period.....	2,247	2,578
Net (loss) income and comprehensive (loss) income attributable to non-controlling interest.....	(45)	104
Distributions.....	<u>(341)</u>	<u>(359)</u>
Balance—end of period.....	<u>1,861</u>	<u>2,323</u>
Common shares and additional paid-in capital		
Balance—beginning of period.....	2,717,633	2,716,798
Issuance of 89,024 and 201,512 common shares.....	348	479
Share-based compensation.....	<u>181</u>	<u>66</u>
Balance—end of period.....	<u>2,718,162</u>	<u>2,717,343</u>
Accumulated deficit		
Balance—beginning of period.....	(2,085,637)	(2,061,854)
Net income (loss) attributable to controlling interest.....	53,041	(8,777)
Accounting effect of the purchase of Series B perpetual non-cumulative preference shares.....	(57,300)	-
Cumulative effect of change in accounting principle for equity securities.....	-	7,469
Balance—end of period.....	<u>(2,089,896)</u>	<u>(2,063,162)</u>
Accumulated other comprehensive income		
Balance—beginning of period.....	1,828	31,015
Other comprehensive income (loss) attributable to controlling interest.....	10,007	(13,071)
Cumulative effect of change in accounting principle for equity securities.....	<u>-</u>	<u>(7,469)</u>
Balance—end of period.....	<u>11,835</u>	<u>10,475</u>
Total common shareholders' equity—end of period.....	<u>640,101</u>	<u>664,656</u>
Total shareholders' equity—end of period.....	<u>\$ 647,775</u>	<u>\$ 680,432</u>

See accompanying Notes to Unaudited Consolidated Financial Statements.

SYNCORA HOLDINGS LTD.
CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)
THREE MONTHS ENDED MARCH 31, 2019 AND 2018
(U.S. dollars in thousands)

	2019	2018
Cash flows from operating activities:		
Premiums collected.....	\$ 577	\$ 1,956
Investment income collected.....	9,483	11,490
Fees received on credit default swaps.....	482	1,016
Claims paid to policyholders and loss adjustment expenses paid.....	(2,310)	(74,780)
Cash received from settlement.....	-	301,406
Operating expenses paid.....	(19,675)	(25,005)
Income taxes paid.....	(496)	-
Other cash receipts.....	1,316	15,502
Cash paid for insurance cash flow certificates.....	-	(77)
Cash received on insurance cash flow certificates.....	-	1,133
Investment income collected by variable interest entities.....	1,468	19,116
Interest and other expenses paid by variable interest entities.....	(37)	(2,665)
Net cash (used in) provided by operating activities from continuing operations.....	(9,192)	249,092
Net cash used in operating activities from discontinued operations.....	-	(539)
Net cash (used in) provided by operating activities.....	(9,192)	248,553
Cash flows from investing activities:		
Proceeds from sales of investments.....	42,512	67,773
Proceeds from maturity of investments.....	17,725	10,408
Net proceeds of short-term securities.....	4,367	22,004
Purchases of investments.....	(72,166)	(16,360)
Net proceeds from consolidated variable interest entities' assets.....	271	32,795
Net cash (used in) provided by investing activities from continuing operations.....	(7,291)	116,620
Net cash used in investing activities from discontinued operations.....	-	(183)
Net cash (used in) provided by investing activities.....	(7,291)	116,437
Cash flows from financing activities:		
Net paydowns of consolidated variable interest entities' liabilities.....	-	(8,340)
Purchase of Series B perpetual non-cumulative preference shares.....	(64,940)	-
Distributions to non-controlling interest in consolidated entity.....	(341)	(359)
Net cash used in financing activities from continuing operations.....	(65,281)	(8,699)
Net cash used in financing activities.....	(65,281)	(8,699)
(Decrease) increase in cash and cash equivalents and restricted cash.....	(81,764)	356,291
Cash and cash equivalents and restricted cash and cash equivalents—beginning of period.....	161,020	351,434
Cash and cash equivalents and restricted cash and cash equivalents—end of period.....	\$ 79,256	\$ 707,725
Summary of cash and cash equivalents and restricted cash and cash equivalents- end of period:		
Cash and cash equivalents.....	\$ 65,557	\$ 670,588
Restricted cash and cash equivalents.....	13,699	1,013
Cash and cash equivalents included in assets of entity held-for-sale.....	-	35,935
Restricted cash included in assets of entity held-for-sale.....	-	189
Cash and cash equivalents and restricted cash and cash equivalents—end of period.....	\$ 79,256	\$ 707,725
Supplemental non-cash transactions:		
Deconsolidation of variable interest entities.....	\$ -	\$ 35,207
Net (receivable) payable for securities.....	(3,734)	991

See accompanying Notes to Unaudited Consolidated Financial Statements.

SYNCORA HOLDINGS LTD.
CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)
THREE MONTHS ENDED MARCH 31, 2019 AND 2018
(U.S. dollars in thousands)

	2019	2018
Reconciliation of income (loss) from continuing operations to net cash (used in) provided by operating activities from continuing operations:		
Income (loss) from continuing operations.....	\$ 52,996	\$ (15,539)
Adjustments to reconcile income (loss) from continuing operations to net cash (used in) provided by operating activities from continuing operations:		
Depreciation and amortization.....	261	261
Net unrealized and realized gains on investments.....	(6,681)	(996)
Unrealized losses on credit default and other swap contracts.....	1,947	21,903
Net change in variable interest entities.....	(290)	(1,870)
Foreign currency exchange gain.....	(640)	(1,308)
Amortization (accretion) on insurance cash flow certificates.....	13,735	(34,333)
Other operating activities.....	5,690	20,386
Changes in assets and liabilities:		
Premiums receivable (retained and ceded).....	(233)	2,350
Prepaid reinsurance (ceded).....	3,418	-
Deferred acquisition costs and deferred loss on reinsurance, net (retained).....	533	2,314
Salvage and subrogation recoverable (retained).....	(20,858)	293,156
Reinsurance recoverable on unpaid losses and loss adjustment expenses (ceded).....	3,322	-
Other assets.....	(5,579)	3,286
Unpaid losses and loss adjustment expenses (retained and ceded).....	(56,588)	(31,214)
Unearned premium revenue (retained and ceded).....	(4,204)	(17,385)
Reinsurance premiums payable (ceded).....	68	-
Notes payable.....	3,235	12,388
Accrued interest on notes payable.....	2,493	12,085
Accounts payable, accrued expenses and other liabilities.....	(1,817)	(16,392)
Total adjustments.....	(62,188)	264,631
Net cash (used in) provided by operating activities from continuing operations.....	\$ (9,192)	\$ 249,092

See accompanying Notes to Unaudited Consolidated Financial Statements.

SYNCORA HOLDINGS LTD.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. Organization and Business

Syncora Holdings Ltd. (“Syncora Holdings”) is a Bermuda holding company, which was formed on March 17, 2006 to provide, through its wholly-owned subsidiary, financial guarantee insurance and reinsurance. Syncora Holdings collectively with its consolidated subsidiaries is hereafter referred to as the (“Company”).

Syncora Holdings’ principal business operating subsidiary is Syncora Guarantee Inc. (“SGI” or “Syncora Guarantee”). SGI collects and expects to continue to collect premiums on existing business; however, SGI ceased writing substantially all new business in January 2008 and is no longer licensed to do so in certain states and other jurisdictions. SGI is an insurance company domiciled in the State of New York, which is regulated by the New York State Department of Financial Services (“NYDFS”) and at one time was licensed to conduct financial guarantee insurance business throughout all 50 of the United States and other jurisdictions.

Prior to January 2008, the Company was primarily engaged in the business of providing (i) credit enhancement on fixed and variable rate debt obligations through the issuance of financial guarantee insurance policies and (ii) credit protection on specific referenced credits or on pools of specific referenced credits through the issuance of financial guarantee insurance policies covering the obligations under credit default swap (“CDS”) contracts issued by trusts established to comply with the New York Insurance Law (the “NYIL”). These trusts are consolidated by the Company.

Financial guarantee insurance policies obligate the insurer to provide an unconditional and irrevocable guarantee to the holder of a debt obligation of full and timely payment of certain principal and interest when due. In the event of a default under the debt obligation, the insurer has recourse against the issuer and/or any related collateral (which is more common in the case of insured asset-backed obligations or other non-municipal debt) for amounts paid under the terms of the policy. CDS contracts are derivative contracts that offer credit protection relating to a particular security or pools of specified securities. Under the terms of a CDS contract, the seller of credit protection makes a specified payment to the buyer of credit protection upon the occurrence of one or more specified credit events with respect to a referenced security. Credit derivatives typically provide protection to a buyer rather than credit enhancement of a debt security as in traditional financial guarantee insurance.

Pike Pointe Holdings, LLC (“Pike Pointe”) is a wholly-owned subsidiary of SGI, which was formed as a Delaware limited liability company to hold certain infrastructure assets, including 100% of the equity ownership of a number of its subsidiaries that previously owned and operated certain toll road facilities located in the United States and Canada (collectively, “American Roads LLC”). On July 16, 2018, the Company closed the sale of American Roads LLC, which is presented as discontinued operations (see Note 16 for further discussion).

The Company has one reportable operating business segment, which is Financial Guarantee Insurance. The Company’s financial guarantee business segment is conducted primarily through SGI.

Closing of Reinsurance Agreement with Assured Guaranty Corp.

On June 1, 2018, SGI closed a reinsurance transaction with Assured Guaranty Corp. (“Assured”) pursuant to which Assured agreed to provide reinsurance, generally on a 100% quota share basis, to SGI of approximately \$12.1 billion of net par outstanding of SGI-insured financial guaranty insurance policies, representing approximately 92% of SGI’s outstanding insured exposure. As consideration for the transaction, which also involved a commutation of a small book of business ceded to SGI by an Assured affiliate which is included in the par outstanding numbers above, SGI paid approximately \$360 million (which amount includes ceded reserves) and assigned over future installment premium for the reinsured policies. In addition, SGI exercised its option to cede certain debt service reserve fund surety and interest rate swap policies for an additional premium payment of \$2.3 million. Subsequent to the execution of this reinsurance agreement, SGI’s remaining insured portfolio was approximately \$1.1 billion of net par outstanding as of June 30, 2018. In addition, in connection with the reinsurance, SGI entered into an administrative services agreement with Assured pursuant to which Assured will provide certain administrative services with respect to the reinsured policies, including surveillance activities and the obligation to administer and pay claims on behalf of SGI. The Company entered into with Assured a credit agreement and related security agreement, pursuant to which Assured agreed to make loans to the Company to fund its claims payments on remediated residential mortgage-backed securities (“RMBS”). See Note 14 for collateral requirements.

2. Description of Significant Risks and Uncertainties and Description of the Company's On-Going Strategic Plan

Significant Risks and Uncertainties

Syncora Holdings is a holding company with no operations or significant assets other than \$5.0 million of debt securities and cash and cash equivalents and its common equity ownership of its subsidiaries as of March 31, 2019. Syncora Holdings' only potential sources of funds are dividends and/or reimbursements for certain expenses related to the general services agreement with its subsidiaries to provide funds for its working capital needs and to pay operating expenses. The remainder of its capital is held at SGI, and any dividends and/or distributions from SGI are subject to regulatory prohibitions and limitations and to the prior claims of its preferred shareholders. There can be no assurance that Syncora Holdings will be able to maintain adequate capital or have sufficient liquidity in the future to pay its operating expenses. See Note 15 for financial information of Syncora Holdings.

The Company is exposed to significant risks and uncertainties that may materially affect its operations, financial and liquidity position. These relate to, among other things, (i) the performance of Assured under the reinsurance and related agreements, (ii) the potential for future adverse loss and claims development on its insured obligations or salvage and (iii) the amount or timing of anticipated recoveries of Puerto Rico related remediation bonds and salvage on related claims payments. These risks and uncertainties are discussed more fully below and could materially and adversely affect the Company's results of operations, financial condition and liquidity.

Description of Significant Risks and Uncertainties and Other Matters

- Effective June 1, 2018, the Company entered into with Assured (i) a reinsurance agreement, pursuant to which the Company ceded \$12.1 billion of its insured exposure, (ii) an administrative services agreement pursuant to which Assured will provide certain administrative services with respect to the reinsured policies, including reporting and making claims payments, and (iii) a credit agreement and related security agreement, pursuant to which Assured agreed to make loans to the Company to fund its claims payments on remediated RMBS. As a result of the reinsurance transaction, the Company is exposed to reinsurance counterparty credit risk that the reinsurer may default in its financial obligations with respect to the terms of the reinsurance agreement. This credit risk could cause increased losses and loss reserves and a reduction in reinsurance recoverables. In addition, the failure of Assured to perform under the administrative services agreement or the credit agreement could cause a disruption to the Company's insurance operations and could increase operational costs and the Company's liquidity needs.
- As of March 31, 2019, the Company has \$288.9 million of net exposure to Puerto Rico (excluding interest outstanding of \$59.9 million), which includes direct insurance and reinsurance of bond policies, direct investments by the Company as a result of remediation transactions and salvage and subrogation rights on the Puerto Rico related claims payments. This exposure relates primarily to bonds issued by the Puerto Rico Electric Power Authority ("PREPA") of \$164.2 million (excluding interest outstanding of \$30.1 million) and general obligation bonds of the Commonwealth of Puerto Rico (the "Commonwealth") of \$102.7 million (excluding interest outstanding of \$21.8 million) and \$22.0 million of net exposure to other obligations of Puerto Rico (excluding interest outstanding of \$8.0 million). As of March 31, 2019, the Company paid approximately \$201.9 million in net claims, representing principal and interest due related to Commonwealth and PREPA exposures. Given that the Puerto Rico proceedings under PROMESA (as detailed below) may continue for an extended period, the Company may be required to make further material claims payments and therefore further increase the proportion of its assets that are comprised of salvage and subrogation rights. Recoveries relating to these rights and interests could be long-dated, which could have a material adverse effect on the Company's short-term liquidity needs. During 2018, the Company had sold approximately \$108.3 million consisting of principal and interest of its salvage and subrogation rights related to these exposures.

On June 30, 2016, the President enacted the Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA"), which provides Puerto Rico and its instrumentalities with both an in-court (Title III) and out-of-court (Title VI) process to restructure debts and bind holdouts. PROMESA provides for the establishment of an Oversight Board, which the President appointed on August 31, 2016, with the authority to approve adjustments of debt of Puerto Rico and its instrumentalities, including PREPA.

On May 3, 2017, the Oversight Board filed a petition under Title III on behalf of the Commonwealth. On June 27, 2017, the Oversight Board voted to reject the PREPA Restructuring Support Agreement (the "RSA"), which resulted in the termination of the RSA on June 29, 2017. On July 2, 2017, the Oversight Board filed a petition under Title III on behalf of PREPA. The Commonwealth's and PREPA's Title III proceedings increase the risk and uncertainty relating to the ultimate recovery on the Commonwealth's general obligations bonds and of PREPA's power revenue bonds.

SYNCORA HOLDINGS LTD.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

On June 14, 2017, the judge overseeing the Title III proceedings entered an order appointing a team of mediators to facilitate confidential settlement negotiations of any issues arising in those proceedings. The Company is participating in the mediation process.

On September 20, 2017, Hurricane Maria made landfall on Puerto Rico causing extensive and widespread damage to property and infrastructure, including loss of electric power throughout the island. The Oversight Board certified a revised fiscal plan for PREPA on August 1, 2018 and for the Commonwealth on October 23, 2018, which are intended to provide the bases for any plans of adjustment in the Title III cases of PREPA and the Commonwealth. Additional revisions to the certified fiscal plans are currently in process.

On June 5, 2018, agents representing the Commonwealth and the Puerto Rico Sales Tax Financing Corp (“COFINA”) disclosed an agreement in principle resolving the ownership dispute between the Commonwealth and COFINA over the Commonwealth’s sales and use tax. On August 8, 2018, the Oversight Board, the Governor and the COFINA creditors announced the terms of a consensual Title III plan of adjustment for COFINA, which is premised on the earlier settlement regarding the sales and use tax. On October 19, 2018, the Oversight Board filed the COFINA plan of adjustment and the settlement agreement allocating the Commonwealth’s sales and use tax. These agreements do not allocate distributions among Commonwealth creditors, including holders of insured general obligation bonds. The Title III court approved the settlement agreement and confirmed the COFINA plan of adjustment on February 4, 2019, which went effective on February 12, 2019.

On July 30, 2018, the Oversight Board announced that it entered into a preliminary restructuring support agreement with the ad hoc group of PREPA bondholders, PREPA and the Commonwealth. This agreement contemplates the exchange of outstanding uninsured PREPA bonds for two classes of new securitization bonds and does not address the treatment of insured PREPA bonds.

On February 15, 2019, the U.S. Court of Appeals for the First Circuit issued an opinion finding that the members of the Oversight Board were not appointed in compliance with the appointments clause of the U.S. Constitution, but declined to dismiss the Title III petitions previously filed by the Oversight Board and delayed the effectiveness of its ruling for 90 days so as to allow the President and the Senate to validate the current appointments or reconstitute the Oversight Board in accordance with the appointments clause. On April 23, 2019, the Oversight Board filed a petition with the U.S. Supreme Court to review the First Circuit’s decision and also requested that the First Circuit stay its ruling, pending the Supreme Court’s final disposition of the case. On March 6, 2019, the First Circuit denied the Oversight Board’s request to stay its mandate, but agreed to delay the effectiveness of its ruling until July 15, 2019.

On April 9, 2019, the Oversight Board, PREPA and the Commonwealth announced that they had reached an agreement in principle for a definitive restructuring support agreement with Assured Guaranty Corp., Assured Guaranty Municipal Corp. and the ad hoc group of PREPA bondholders, which supersedes the July 2018 preliminary restructuring support agreement. On May 10, 2019, the Oversight Board filed a motion to approve the definitive restructuring support agreement and a hearing on that motion is currently scheduled for June 12, 2019. The definitive restructuring support agreement does not address the treatment of the Company insured PREPA bonds.

On May 2, 2019, the Oversight Board and the official committee of unsecured creditors filed a complaint challenging numerous proofs of claims relating to general obligation bonds, including those filed by the Company. Among other things, the complaint disputes the existence, extent, and enforceability of the consensual and statutory liens asserted in the proofs of claim and is seeking to reclassify such claims as unsecured obligations of the Commonwealth.

Due to the pending Title III cases, the Company may experience further losses on these insured obligations which could have a material adverse effect on the Company’s liquidity and financial position.

- As of March 31, 2019, in respect of its Puerto Rico-related exposure, the Company has made substantial claim payments and anticipates that it may be requested to make further gross claim payments in the period 2019 to 2029 of at least approximately \$97.5 million, followed in later years (in some cases significantly later years) by recoveries of salvage made in respect of these claims payments. The amount and timing of the salvage recoveries related to all of these claims payments are subject to greater uncertainty than the amount and timing of such future claims payments themselves. Pursuant to the Company’s accounting policy and guidance under Generally Accepted Accounting Principles (“GAAP”), the net present value of estimated claims and recoveries (including salvage and subrogation) are reflected in the Company’s loss reserves and salvage and subrogation recoverable (see Note 5). Because of the inherent uncertainty in estimating future claim payments and recoveries, no assurance can be given that the amount or timing of claims payments, related recoveries, or ultimate losses match the Company’s estimates, and such differences could materially and adversely affect the Company’s results of operations, financial condition and liquidity. The Company may also experience significant adverse development on its insured obligations that may place further demands on

SYNCORA HOLDINGS LTD.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

the Company's liquidity and financial position. See Note 5 "*Schedule of Insured Financial Obligations with Credit Deterioration*" caption for further discussion.

- The Company and its financial position will continue to be subject to risk of global financial and economic conditions that could materially and adversely affect the amount of potential losses (including the timing and amount of potential claims and subsequent recoveries) incurred on transactions it guarantees, the value of its investment portfolio, and otherwise materially and adversely affect the Company. With respect to the Company's investment portfolio, a prolonged period of low interest rates, along with declining investment balances, may adversely affect the Company's ability to generate sufficient investment income to fund its future obligations. Issuers or borrowers whose securities or loans the Company insures or holds as well as the Company's counterparties under swaps and other derivative contracts may default on their obligations to the Company due to bankruptcy, insolvency, lack of liquidity, adverse economic conditions, operational failure, fraud or other reasons. Additionally, the underlying assets supporting securities that the Company has guaranteed may deteriorate further, causing these securities to incur losses.
- The Company has direct insurance and reinsurance exposure to certain credits within European countries. Global economic conditions have been negatively affected with concerns about the continued sovereign debt crisis within the European region and the possibility that certain European Union member states will default on their debt obligations or leave the European Union. The continued uncertainty over the outcome of the European Union governments' efforts to provide financial support for sovereigns and sub-sovereigns and the possibility of further deteriorating conditions in Europe could have a material adverse effect on the Company's financial and liquidity position. As of March 31, 2019, the Company's net in-force guaranteed principal exposure to the European Union was approximately \$490.6 million of which \$256.2 million of exposure is to credits in the UK and denominated in British Pound sterling and \$234.4 million was specifically related to certain credits in higher risk countries, such as Portugal and Italy.
- The Financial Conduct Authority of the United Kingdom plans to phase out the London Interbank Offered Rate ("LIBOR") by the end of 2021. LIBOR is the benchmark rate that many banks and issuers use to set interest rates in loan documents. United States' authorities recognizing the need for a LIBOR replacement, convened the Alternative Reference Rate Committee ("ARRC") in 2014 to find a replacement. After three years of study the ARRC identified the Secured Overnight Financing Rate ("SOFR") – the broadest of three existing Repo rates, as its preferred alternative to LIBOR. The Company has LIBOR based gross and net par outstanding insured exposure of \$292.5 million and \$1.3 million, respectively. An increase in interest rates, the potential phase out of LIBOR and the difference between LIBOR and SOFR could have a material adverse effect on the Company's liquidity and financial position.
- The Company is materially exposed to foreign exchange risk as the Company's insured debt obligations are denominated in a number of foreign currencies and the U.S. dollar. The principal currencies creating foreign exchange risk are the British Pound sterling and the European Union euro. At March 31, 2019, approximately 53% of the Company's in-force guaranteed net par outstanding exposure of \$0.9 billion was denominated in such currencies. The Company translates foreign currencies into U.S. dollars at the current market exchange rates. Changes in the exchange rates between foreign currencies and U.S. dollars may have an adverse effect on the settlement of potential claims or the value of salvage/recoveries and therefore could have a material adverse effect on the Company's liquidity and financial position. In addition, the Company is materially exposed to risks associated with its financial guarantees covering foreign denominated inflation indexed-linked bonds in connection with the bonds issued by UK and European utility and project finance issuers.
- Establishment of case basis reserves for unpaid losses and loss adjustment expenses on the Company's in-force business requires the use and exercise of significant judgment and is based on certain assumptions made by management, including estimates regarding the likelihood of occurrence, timing and amount of a loss on a guaranteed obligation. Changes in such assumptions could materially adversely affect such reserve estimates, including the amount and timing of any claims. Under certain conditions, many of which are event-driven and outside the control of the Company, these exposures may result in significant increases in claims beyond those assumed in the Company's reserve estimate (that may or may not result in an increase in such loss reserves) in the near to medium term. A material portion of the Company's case basis reserves reflects certain assumptions that affect reimbursements in the remainder of its insured and reinsured portfolio. Actual experience may, and likely will, differ from those estimates and such difference may be material due to the fact that the ultimate dispositions of claims are subject to the outcome of events that have not yet occurred and, in certain cases, will occur over many years in the future. Examples of these events include changes in the level of interest rates, credit deterioration of guaranteed obligations, recoveries in bankruptcy proceedings, changes in the value of specific assets supporting guaranteed obligations and changes in the level of investment yield. Both qualitative and quantitative factors are used in making such estimates. From time to time the Company reevaluates all such estimates, which may be material. Any estimate of future costs is subject to the inherent limitation on management's ability to predict the aggregate

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course of future events. It should, therefore, be expected that the actual emergence of losses and claims will vary, perhaps materially, from any estimate. The risk of loss under the Company's guarantees extends to the full amount of unpaid principal and interest on all debt obligations it has guaranteed.

- SGI has sought, and may in the future seek, the NYDFS's approval of permitted accounting practices and other regulatory relief which have, and if granted may have, a material effect on SGI's statutory policyholders' surplus. Once granted, these permitted accounting practices have been subject to an annual approval or confirmation. No assurance can be given that the NYDFS will continue to grant approval of SGI's past or any future permitted accounting practices or requested regulatory relief. Failure to obtain continuing approval of the past or future permitted accounting practices or requested regulatory relief could have a material adverse effect on SGI's statutory policyholders' surplus.
- Should the Company experience an "ownership change" for purposes of Section 382 of the Internal Revenue Code, the Company's ability to utilize its net operating loss carryforwards could be subject to an annual limitation in the future, which would be expected to result in a material increase in the Company's U.S. federal income tax liability, reduce reimbursements from profitable affiliates under its tax sharing agreement and therefore materially adversely affect the Company's equity and liquidity position. While the Syncora Holdings Ltd. bye-laws contain restrictions intended to reduce the likelihood of such an "ownership change," it remains possible that an "ownership change" could nonetheless occur. These limitations may prevent Syncora Holdings Ltd. from taking certain strategic actions or may make it more difficult for Syncora Holdings Ltd. to attract additional capital. In addition, although the Company has not taken any uncertain tax positions, the IRS may nonetheless disagree with the Company's interpretation of this and other tax related matters.
- Notwithstanding the repayment in full of the Company's surplus notes, and the restructuring transactions completed on August 12, 2016 as discussed in Note 3, the Company remains subject to certain regulatory restrictions that limit its financial and operating flexibility and may materially and adversely impair its ability to execute on its strategic plan. See below Description of the Company's On-Going Strategic Plan and associated risks.
- The Company's ability to pay dividends on its preferred and common shares is subject to risks and uncertainties, including, without limitation, prior regulatory approval by the NYDFS. No assurance can be given as to whether or when SGI may be able to pay any dividends on its preferred and/or common shares, or whether or when its preferred shares may be redeemed. As discussed in Note 13, SGI's ability to pay dividends is subject to regulatory constraints.
- The Company is involved in legal proceedings. Management cannot predict the outcomes of these legal proceedings with certainty. A favorable outcome could have a material effect on the Company's financial and liquidity position. Prosecuting these legal proceedings involves significant expense and diversion of management's attention and resources from other matters.
- The Company relies upon information technology and systems, including those of third parties, to support a variety of its business processes and activities. In addition, the Company has collected and stored confidential information. The Company's data systems and those of third parties on which it relies may be vulnerable to security breaches from external and internal factors. Problems in, or security breaches of, these systems could result in, among other things, reputational harm, the disclosure or misuse of confidential or proprietary information, inaccurate loss projections, legal costs and regulatory penalties. As the Company's business operations rely on the continuous availability of its computer systems, as well as those of certain third parties, a failure to maintain business continuity in the wake of disruptive events could prevent the timely completion of critical processes across its operations, including, for example, claims processing and investment operations. These failures could result in additional costs, fines and litigation.
- Syncora Holdings' business could be negatively affected as a result of actions of activist stockholders, and such activism could affect the trading value of its securities. Responding to actions by activist stockholders can be costly and time-consuming, disrupting operations and diverting the attention of management and employees. Such activities could interfere with management's ability to execute its strategic plan. In addition, a proxy contest for the election of directors at the Company's annual meeting would require Syncora Holdings to incur significant legal fees and proxy solicitation expenses and require significant time and attention by management and board of directors. The perceived uncertainties as to Syncora Holdings' future direction also could affect the market price and volatility of its securities.
- The Company's success substantially depends upon its ability to retain qualified employees and upon the ability of its senior management and other key employees to implement its strategic plan. The Company relies substantially upon the services of its executive team and other key employees. The loss of the services of any of these individuals or other key members of the Company's management team or the inability to hire talented personnel could adversely affect the implementation of its strategic

plan or ability to operate the business.

The Company may be unable to execute any or all of the elements of its On-Going Strategic Plan on a timely basis or at all, as described below.

Description of the Company's On-Going Strategic Plan

On March 4, 2019, the Company announced that its Board of Directors has commenced a formal review process to explore and evaluate strategic alternatives for the Company focused on optimizing shareholder value and returning capital to shareholders. These alternatives include, among other things, a sale of part or all of the Company or its wholly-owned, New York financial guarantee insurance subsidiary, Syncora Guarantee.

Furthermore, the Company, together with its subsidiaries, continues to pursue certain key initiatives in order to continue to deliver enhanced value to stakeholders. These initiatives include (i) continuing to focus on reducing the Company's retained insured exposures (through their purchase on the open market or otherwise, commutation, defeasance, reinsurance or other restructuring) to minimize potential claim payments, maximize recoveries and mitigate potential losses, (ii) continuing to evaluate when and how to utilize NOLs that were reallocated to Syncora Holdings US Inc. as part of the restructuring transaction completed on August 12, 2016, (iii) seeking to realize the maximum value of its assets, and from any other rights and remedies the Company may have, (iv) transitioning services to Assured in respect of the reinsurance agreement and the administrative services agreement, (v) seeking to novate or purchase with a view towards novating to Assured, the policies reinsured to Assured, and (vi) further reducing operating expenses and improving operational efficiencies.

Any or all of these actions may be outside the ordinary course of the Company's operations or its control and may require consents, approvals or cooperation of third parties, including the NYDFS, and there can be no assurance that any such consents, approvals or cooperation will be obtained on a timely basis or at all.

3. Completion of Restructuring Transactions and the 2009 MTA and Related Transactions

Description of the 2016 Restructuring Transactions

On August 12, 2016, Syncora Holdings US Inc., a wholly-owned subsidiary of Syncora Holdings, completed, among other things, a surplus note exchange offer and proxy solicitation for the variation of rights to the SHL Preferred Shares, which upon closing, cancelled all of the Syncora Holdings preferred shares outstanding.

Description of the 2009 MTA

On April 30, 2019, the Company paid its surplus notes in full. Following payment in full, the following restrictions in its master transaction agreement with certain of its financial counterparties to CDS contracts insured by the Company's financial guaranty insurance policies and certain related transactions (referred to collectively as the "2009 MTA") no longer apply: the Company may not (i) make any distribution, pay, redeem, repurchase, retire, exchange or otherwise acquire its surplus notes, except on a pro rata basis and on the same terms; (ii) merge, consolidate or sell, assign, transfer or dispose of all or any material portion of its assets; (iii) pay any dividend, repurchase, redeem, exchange or convert any of its equity securities (or of any of its direct or indirect parent); (iv) issue any surplus notes; or (v) incur any indebtedness. Accordingly, the restrictive covenants in the 2009 MTA are no longer operative.

4. Significant Accounting Policies

Specific accounting policies pertaining to insurance operations, investments, debt and discontinued operations are disclosed within the applicable notes to the consolidated financial statements.

Basis of Presentation

The accompanying unaudited interim consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States ("GAAP") for interim financial information. In the opinion of management, all adjustments (consisting of normal recurring accruals and the use of estimates) considered necessary for a fair presentation pursuant to these requirements have been included. Actual results could differ from those estimates. The results of operations for any interim period are not necessarily indicative of the results for a full year.

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Consolidation

The consolidated financial statements include the accounts of the Company, its wholly-owned subsidiaries and all other entities in which the Company has a controlling financial interest, including VIEs for which the Company is deemed to be the primary beneficiary. All intercompany accounts and transactions have been eliminated.

Reclassifications

Certain reclassifications were made to prior period consolidated financial statement amounts to conform to the current period presentation. There were no effects on net income or shareholders' equity as a result of these reclassifications.

Other Income and Fees

Other income and fees include waiver, consent, termination and other fees in connection with certain of the Company's insured transactions, in addition to other miscellaneous sources of income. Depending upon the type of fee received, the fee is either earned when services are rendered and the fee is due, or deferred and earned over a stipulated period or the life of the related transaction.

Operating Expenses

Operating expenses primarily include compensation and employee benefits, professional and legal fees, computer related costs, rent and occupancy costs, depreciation and amortization expense, administrative services agreement fees, foreign currency exchange losses and other general and administrative expenses.

Foreign Currency Translation

Assets and liabilities denominated in foreign currencies are translated into U.S. dollar equivalents at exchange rates prevailing as of the date of the consolidated balance sheet. Revenues and expenses are translated at average exchange rates prevailing during the period. Gains and losses resulting from foreign currency transactions to U.S. dollar equivalents are recorded in current income and reflected in the operating expenses caption in the consolidated statements of operations.

Earnings Per Share

Basic earnings per share amounts are calculated by dividing earnings attributable to common shareholders by the weighted average number of common shares outstanding during the period, excluding the effect of dilutive securities. Diluted earnings per share amounts are calculated by dividing earnings attributable to common shareholders by the sum of the weighted average number of common shares outstanding during the period plus additional shares potentially issued from all dilutive securities. There were no dilutive securities outstanding at March 31, 2019 and December 31, 2018, respectively.

Recent Accounting Pronouncements

Recently Adopted Accounting Pronouncements

In March 2017, the FASB issued "Receivables-Nonrefundable Fees and Other Costs - Premium Amortization on Purchased Callable Debt Securities". This standard shortens the amortization period for the premium on callable debt securities to the earliest call date. Currently under GAAP, a reporting entity generally amortizes the premium as yield adjustment over the contractual or maturity life of the debt security and if such debt security is called, the entity would record a loss equal to the unamortized premium. This standard does not change the accounting for callable debt securities held at a discount, which will continue to be amortized to maturity. The Company adopted this standard as of January 1, 2019 and the adoption of this standard did not have a material effect on the Company's consolidated financial statements.

Accounting Pronouncements Pending Adoption

In June of 2016, the FASB issued "Financial Instruments-Credit Losses: Measurement of Credit Losses on Financial Instruments." This standard introduces a new model for recognizing credit losses on financial instruments based on an estimate of current expected credit losses. This standard applies to financial assets measured at amortized cost, debt securities and other financial assets measured at fair value through other comprehensive income, loans, receivables and certain other financial instruments. This standard requires that financial assets measured at amortized cost be presented at the net amount expected to be collected by recording a valuation allowance, with changes in the allowance reflected in the income statement each period. For available for sale debt securities, credit losses should also be recorded through a valuation allowance, limited to the difference between the fair value and amortized cost of the security. This standard is effective for fiscal years beginning after December 15, 2019 for public business

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enterprises that are Securities and Exchange Commission (“SEC”) filers and after December 15, 2020 for public business enterprises that are non-SEC filers. The Company is evaluating the effect of adopting this standard.

5. Insurance Operations

Premiums Receivable and Unearned Premium Revenue

The Company recognizes a liability for unearned premium revenue at the inception of financial guarantee insurance and reinsurance contracts on a contract-by-contract basis. Unearned premium revenue recognized at inception of a contract is measured at the present value of the premium due or expected to be collected. For certain financial guarantee insurance contracts, the Company receives the entire premium due at the inception of the contract, and recognizes unearned premium revenue liability at that time. For other financial guarantee contracts, the Company receives premiums in installments over the term of the contract at stipulated due dates. Unearned premium revenue and a receivable for future premiums are recognized at the inception of an installment contract, and measured at the present value of premiums expected to be collected over the contract period or expected period using a risk-free discount rate that considers the expected maturity of each contract. The expected period is used in the present value determination of unearned premium revenue and receivable for future premiums for contracts where (a) the insured obligation is contractually prepayable, (b) prepayments are probable, (c) the amount and timing of prepayments are reasonably estimable, and (d) a homogenous pool of assets is the underlying collateral for the insured obligation. The Company has determined that substantially all of its installment contracts are required to be measured based on the contract period. The receivable for future premiums is reduced as installment premiums are collected. The Company reports the accretion of the discount on installment premiums receivable as premium revenue. The Company assesses the receivable for future premiums for collectability each reporting period, adjusts the receivable for uncollectible amounts and recognizes any write-off as an operating expense.

Premium Revenue Recognition

Financial guarantee insurance and reinsurance enterprises recognize the premium from a financial guarantee insurance contract as revenue over the period of the contract in proportion to the amount of insurance protection provided. As premium revenue is recognized, a corresponding decrease in the unearned premium revenue occurs. The amount of insurance protection provided is a function of the insured exposure outstanding. Therefore, the proportionate share of premium revenue to be recognized in a given reporting period is a constant rate calculated based on the relationship between the insured exposure outstanding in a given reporting period compared with the sum of each of the insured exposure amounts outstanding for all periods.

The Company’s accounting policies for the recognition of ceded premiums, ceding commissions and ceded losses and loss adjustment expenses under its ceded reinsurance contracts mirror the policies described herein for premium revenue recognition, deferred ceding commissions, and reserves for losses and loss adjustment expenses.

When an insured issue is retired early, is called by the issuer or is in substance paid in advance through a refunding accomplished by placing U.S. Government securities in escrow, any remaining unearned premium revenue is earned at that time, since there is no longer risk to the Company. Also, premiums earned may be accelerated as a result of the Company’s remediation transactions, which result in the Company no longer being at risk (hereafter collectively with refunding referred to as “Premium Accelerations”).

Reinsurance

Reinsurance premiums ceded are earned over the period the reinsurance coverage is provided. Prepaid reinsurance premiums represent the portion of premiums ceded which is applicable to the unexpired term of reinsured policies in-force. Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liability associated with the reinsured policy. Provision is made for any estimated uncollectible reinsurance.

Insurance Premiums

As of March 31, 2019, the Company reported gross and retained premium receivable of \$56.9 million and \$14.4 million, respectively, primarily related to installment policies for which premiums will be collected over the term of the contracts. The weighted average risk-free rate used to discount future installment premiums was 2.8% and the weighted average collection term of the premium receivable was 11.0 years. For the three months ended March 31, 2019, the accretion of the premium receivable was \$0.4 million and is reported in “Premiums earned” on the accompanying consolidated statement of operations. As of March 31, 2019, the Company reported a reinsurance premium payable of \$42.5 million, which represents the portion of the Company’s premium receivable that is due to reinsurers. The reinsurance premium payable will be accreted and paid, as premiums due to the Company are accreted and collected.

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The following tables present a roll forward of the Company's premium receivable and unearned premium net liability for the three months ended March 31, 2019 and 2018:

(U.S. dollars in thousands)	Retained business		Ceded business		Total	
Three months ended March 31,	2019	2018	2019	2018	2019	2018
Recognition of unearned premium reserve, including commutations and other changes in policy terms	\$ 786	\$ 13,962	\$ 3,418	\$ 3,423	\$ 4,204	\$ 17,385
Reduction in previously written premiums and reinsurance	(243)	(160)	(57)	(1,913)	(300)	(2,073)
Accretion of premium receivable discount	92	501	325	78	417	579
Premiums earned, including net premium accelerations of zero and \$9,580	\$ 635	\$ 14,303	\$ 3,686	\$ 1,588	\$ 4,321	\$ 15,891
Three months ended March 31,	2019	2018	2019	2018	2019	2018
Premiums collected	\$ (312)	\$ (1,738)	\$ (265)	\$ (218)	\$ (577)	\$ (1,956)
Accretion of premium receivable discount	92	501	325	78	417	579
Policy commutations and other changes in policy terms	385	949	8	(1,922)	393	(973)
Change in premiums receivable	165	(288)	68	(2,062)	233	(2,350)
Premium receivable, beginning of period	14,260	79,903	42,458	12,921	56,718	92,824
Premium receivable, end of period	\$ 14,425	\$ 79,615	\$ 42,526	\$ 10,859	\$ 56,951	\$ 90,474
Three months ended March 31,	2019	2018	2019	2018	2019	2018
Recognition of unearned premiums, including commutations and other changes in policy terms	\$ (786)	\$ (13,962)	\$ (3,418)	\$ (3,423)	\$ (4,204)	\$ (17,385)
Change in unearned premium revenue	(786)	(13,962)	(3,418)	(3,423)	(4,204)	(17,385)
Unearned premium revenue, beginning of period	28,500	209,320	112,011	15,565	140,511	224,885
Unearned premium revenue, end of period	\$ 27,714	\$ 195,358	\$ 108,593	\$ 12,142	\$ 136,307	\$ 207,500

Note: Activity in the liability reinsurance premiums payable for ceded business mirrors the activity in the ceded business asset above. Activity in the asset prepaid reinsurance for ceded business mirrors the activity in the ceded business liability above.

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The following table presents the Company's installment premiums on business expected to be collected in the future and the periods in which such collections are expected to occur, the expected unearned premium revenue balance and the expected future premium earnings of the Company's in-force business as of and for the periods presented. In addition to that presented in the table below, the Company had installment premiums receivable of \$1.8 million (on a present value basis) and unearned premium revenue of \$4.1 million relating to assumed reinsurance business at March 31, 2019:

(U.S. dollars in thousands)	Expected Collection of Premiums	Unearned Premium Revenue	Expected Premium Earnings			
			Upfront	Installments	Accretion	Total
Retained business						
Three months ended:						
June 30, 2019	\$ 107	\$ 22,136	\$ 367	\$ 226	\$ 90	\$ 683
September 30, 2019	308	21,549	366	222	90	678
December 31, 2019	<u>100</u>	<u>21,000</u>	<u>331</u>	<u>217</u>	<u>89</u>	<u>637</u>
Twelve months ended:						
December 31, 2020	783	18,901	1,267	832	338	2,437
December 31, 2021	738	16,935	1,188	778	316	2,282
December 31, 2022	692	15,107	1,106	722	295	2,123
December 31, 2023	680	13,403	1,010	695	276	1,981
December 31, 2024	<u>672</u>	<u>11,829</u>	<u>902</u>	<u>672</u>	<u>257</u>	<u>1,831</u>
Five years ended:						
December 31, 2029	3,378	6,406	2,290	3,133	993	6,416
December 31, 2034	3,404	2,437	1,172	2,797	502	4,471
December 31, 2039	1,832	208	823	1,406	105	2,334
December 31, 2044	116	-	98	110	2	210
December 31, 2049	-	-	-	-	-	-
December 31, 2054	-	-	-	-	-	-
December 31, 2059	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total	<u>\$ 12,810</u>		<u>\$ 10,920</u>	<u>\$ 11,810</u>	<u>\$ 3,353</u>	<u>\$ 26,083</u>
Ceded business						
Three months ended:						
June 30, 2019	\$ 1,182	\$ 107,390	\$ 1,557	\$ 999	\$ 310	\$ 2,866
September 30, 2019	570	104,885	1,513	993	301	2,807
December 31, 2018	<u>818</u>	<u>102,508</u>	<u>1,390</u>	<u>987</u>	<u>294</u>	<u>2,671</u>
Twelve months ended:						
December 31, 2020	4,039	93,312	5,335	3,862	1,088	10,285
December 31, 2021	3,442	84,855	4,941	3,515	960	9,416
December 31, 2022	3,198	77,281	4,550	3,024	855	8,429
December 31, 2023	3,150	70,233	4,147	2,901	756	7,804
December 31, 2024	<u>3,094</u>	<u>63,717</u>	<u>3,740</u>	<u>2,776</u>	<u>658</u>	<u>7,174</u>
Five years ended:						
December 31, 2029	10,116	39,822	14,831	9,063	2,215	26,109
December 31, 2034	7,007	23,451	10,981	5,390	1,022	17,393
December 31, 2039	2,792	13,249	8,272	1,930	248	10,450
December 31, 2044	454	8,339	4,567	343	58	4,968
December 31, 2049	216	4,473	3,712	154	12	3,878
December 31, 2054	6	673	3,795	5	-	3,800
December 31, 2059	<u>-</u>	<u>-</u>	<u>673</u>	<u>-</u>	<u>-</u>	<u>673</u>
Total	<u>\$ 40,084</u>		<u>\$ 74,004</u>	<u>\$ 35,942</u>	<u>\$ 8,777</u>	<u>\$ 118,723</u>

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(U.S. dollars in thousands)	Expected Collection of Premiums	Unearned Premium Revenue	Expected Premium Earnings			
			Upfront	Installments	Accretion	Total
Total						
Three months ended:						
June 30, 2019	\$ 1,289	\$ 129,526	\$ 1,924	\$ 1,225	\$ 400	\$ 3,549
September 30, 2019	878	126,434	1,879	1,215	391	3,485
December 31, 2018	<u>918</u>	<u>123,508</u>	<u>1,721</u>	<u>1,204</u>	<u>383</u>	<u>3,308</u>
Twelve months ended:						
December 31, 2020	4,822	112,213	6,602	4,694	1,426	12,722
December 31, 2021	4,180	101,790	6,129	4,293	1,276	11,698
December 31, 2022	3,890	92,388	5,656	3,746	1,150	10,552
December 31, 2023	3,830	83,636	5,157	3,596	1,032	9,785
December 31, 2024	<u>3,766</u>	<u>75,546</u>	<u>4,642</u>	<u>3,448</u>	<u>915</u>	<u>9,005</u>
Five years ended:						
December 31, 2029	13,494	46,228	17,121	12,196	3,208	32,525
December 31, 2034	10,411	25,888	12,153	8,187	1,524	21,864
December 31, 2039	4,624	13,457	9,095	3,336	353	12,784
December 31, 2044	570	8,339	4,665	453	60	5,178
December 31, 2049	216	4,473	3,712	154	12	3,878
December 31, 2054	6	673	3,795	5	-	3,800
December 31, 2059	<u>-</u>	<u>-</u>	<u>673</u>	<u>-</u>	<u>-</u>	<u>673</u>
Total	<u>\$ 52,894</u>		<u>\$ 84,924</u>	<u>\$ 47,752</u>	<u>\$ 12,130</u>	<u>\$ 144,806</u>

Deferred Acquisition Costs, Deferred Loss on Reinsurance and Deferred Ceding Commission

Policy acquisition costs include those expenses that primarily relate to, and vary with, the production of new business. These costs include direct expenses related to underwriting, marketing and policy issuance, rating agency fees and premium taxes, and are reduced by ceding commission income on premiums ceded to reinsurers. Policy acquisition costs are deferred and amortized over the period in which the related premiums are earned.

As a result of the reinsurance transaction with Assured discussed above, the Company recorded a deferred loss, which is being amortized over the life of the reinsurance contracts.

For policies reinsured with third parties, the Company receives ceding commissions to compensate for acquisition costs incurred. The Company nets ceding commissions received against deferred acquisition costs and earns these ceding commissions over the period in which the related premiums are earned.

In the event of a Premium Acceleration, the remaining net amount of deferred acquisition costs with respect to refunded insured issue is recognized at such time.

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Deferred acquisition costs, net of deferred ceding commission revenue, as well as related amortization, for the retained business only as of and for the three months ended March 31, 2019 and 2018 are as follows:

(U.S. dollars in thousands)	Retained business	
Three months ended March 31,	2019	2018
Amortization of deferred acquisition costs	\$ 51	\$ 2,324
Amortization of ceding commission revenue	-	(10)
Amortization of deferred loss on reinsurance	482	-
Amortization of deferred acquisition costs, including deferred loss on reinsurance	<u>\$ 533</u>	<u>\$ 2,314</u>
Amortization of deferred acquisition costs, including deferred loss on reinsurance	(533)	(2,314)
Change in deferred acquisition costs, net	(533)	(2,314)
Deferred acquisition costs and deferred loss on reinsurance, net, beginning of period	18,423	34,930
Deferred acquisition costs and deferred loss on reinsurance, net, end of period	<u><u>\$ 17,890</u></u>	<u><u>\$ 32,616</u></u>

Unpaid Loss and Loss Adjustment Expenses

A claim liability (loss reserve) is recognized at the measurement date on a contract-by-contract basis based on the weighted average probability of net cash outflows to be paid under the contract, on a present value basis, to the extent that the claim liability so determined exceeds the unearned premium revenue attributable to such contract at the measurement date.

Establishment of reserves for unpaid losses and loss adjustment expenses requires the use and exercise of significant judgment by management, including estimates regarding the occurrence and amount of a loss on an insured obligation. Actual experience may differ from estimates and such difference may be material, due to the fact that the ultimate dispositions of claims are subject to the outcome of events that have not yet occurred. Examples of these events include changes in the level of interest rates, credit deterioration of insured obligations, and changes in the value of specific assets supporting insured obligations. Both qualitative and quantitative factors are used in establishing such reserves. In determining the reserves, management considers all factors in the aggregate, and does not attribute the reserve provisions or any portion thereof to any specific factor. Any estimate of future costs is subject to the inherent limitation on the Company's ability to predict the aggregate course of future events. It should, therefore, be expected that the actual emergence of losses and loss adjustment expenses will vary, perhaps materially, from any estimate.

The present value of net cash outflows is determined based on a risk free rate of interest commensurate with the expected duration of the related contract. For this purpose, the Company uses the rate on U.S. Treasury obligations with a duration consistent with the duration of the underlying insured obligation for U.S. dollar denominated insured obligations or the comparable risk free rate on foreign government obligations relating to insured obligations denominated in foreign currencies. The weighted average risk free rate at March 31, 2019 and December 31, 2018 was 2.4% and 2.7%, respectively. A claim liability is subsequently remeasured each reporting period for increases or decreases due to changes in the magnitude and likelihood of default and potential recoveries, as well as changes in the risk free rate of interest. Subsequent changes to the measurement of claim liability are recognized as loss expense in the period of change. Measurement and recognition of loss liability is reported gross of any reinsurance. The Company estimates the likelihood of possible claims payments and possible recoveries using probability-weighted expected cash flows based on available information, including market information. Accretion of the discount on a claim liability, as well as any changes in the risk free rate of interest, are included in loss expense.

Loss reserves represent the Company's: (i) probability-weighted average estimate of the net present value of claims to be paid subsequent to the balance sheet date, less (ii) its probability-weighted average estimate of the net present value of recoveries subsequent to the balance sheet date and (iii) any unearned premium revenue relating to such guarantees at the end of the reporting period.

Loss reserves are generally determined using cash flow models to estimate the net present value of the anticipated shortfall between (i) scheduled payments on the insured obligation plus anticipated loss adjustment expenses and (ii) anticipated cash flow from the collateral supporting the obligation and other anticipated recoveries. A number of quantitative and qualitative factors are considered when determining or assessing the need for a case basis reserve. These factors may include the creditworthiness of the underlying issuer of the insured obligation, whether the obligation is secured or unsecured, the projected cash flow or market value of any assets that collateralize or secure the insured obligation, and the historical and projected loss rates on such assets. Other factors that may affect the actual ultimate loss include the state of the economy, changes in interest rates, rates of inflation and the salvage values of specific collateral. Such factors and the Company's assessment thereof will be subject to the specific facts and circumstances associated with the specific insured transaction being considered for loss reserve establishment.

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Loss reserves on financial guarantee reinsurance assumed are generally established by the Company upon quarterly current notifications from a ceding company. There historically has been no time lag between the time the Company records an assumed case basis reserve and the time the Company's ceding company records such reserves. For each notification of a ceded loss reserve from the ceding company, the Company conducts an examination of the basis of the ceding company's reserve estimate to ensure that the Company concurs with the ceding company's evaluation and conclusions. In certain instances, the Company may develop its own estimates of losses on assumed business due to refinements in the assumptions used in the Company's cash flow models based on research and information review. In other cases, when the Company has assumed loss reserves, it has concurred with the ceding company's evaluation and conclusions with respect to such reserves and, accordingly, there has been no difference between the amount of loss reserves reported to the Company by its ceding company and the amount it has recorded in its financial statements.

In assessing reserves for unpaid losses, the Company considers all available qualitative and quantitative evidence. Qualitative evidence may take various forms and the nature of such evidence will depend upon the type of insured obligation and the nature and sources of cash flows to fund the insured obligation's debt service. For example, such evidence with respect to an insured special revenue obligation such as an obligation supported by cash flows from a toll road would consider traffic statistics such as highway volume and related demographic information, whereas an insured mortgage-backed securitization would consider the quality of the mortgage loans supporting the insured obligation including delinquency, default and foreclosure rates, loan to value statistics, market valuation of the mortgaged properties and other pertinent information. In addition, the Company will make qualitative judgments with respect to the amount by which certain other structural protections built into the transaction are expected to limit the Company's loss exposure. Examples of such structural protections may include: (i) rate covenants, which generally stipulate that issuers (i.e., public finance issuers) set rates for services at certain predetermined levels (i.e., water and sewer rates which support debt obligations supported by such revenues), (ii) springing liens, which generally require the issuer to provide additional collateral upon the breach of a covenant or trigger incorporated into the terms of the transaction, (iii) consultant call-in rights, which provide, under certain circumstances, for a consultant to be engaged to make certain binding recommendations, such as raising rates or reducing expenses, (iv) the ability to transfer servicing of collateral assets to another party, and (v) other legal rights and remedies pursuant to representations and warranties made by the issuer and written into the terms of such transactions. Quantitative information may take the form of cash flow projections of the assets supporting the insured debt obligation (which may include, in addition to collateral assets supporting the obligation, structural protections subordinate to the attachment point of the Company's risk, such as cash reserve accounts and letters of credit), as well as (to the extent applicable) other metrics indicative of the performance of such assets and the trends therein. The Company's ability to make a reasonable estimate of its expected loss depends upon its evaluation of the totality of both the available quantitative and qualitative evidence, and no one quantitative or qualitative factor is dispositive.

As of March 31, 2019 and December 31, 2018, the range of risk free rates used to discount the Company's liability for losses and loss adjustment expenses was 0.0% to 2.6% and 0.0% to 2.85%, respectively.

Salvage and Subrogation Recoverable

The Company recognizes a salvage and subrogation recoverable based on net discounted anticipated recoveries in excess of net discounted anticipated paid claims on its financial guaranty insurance contracts up to the amount of previously paid claims or when the Company becomes entitled to the net cash inflows from the underlying collateral of an insured obligation under salvage and subrogation rights as a result of a claim payment or estimated future claim payments. Such recoverable amounts are included in salvage and subrogation recoverable on the accompanying consolidated balance sheets.

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Activity in the Company's liability for unpaid losses and loss adjustment expenses and net liability for the three months ended March 31, 2019 and 2018 are summarized as follows:

(U.S. dollars in thousands)	Retained business		Ceded business		Total	
Three months ended March 31,	2019	2018	2019	2018	2019	2018
Accretion of reserve discount	\$ 1,818	\$ 3,784	\$ 859	\$ -	\$ 2,677	\$ 3,784
Change in reserve discount rates	5,254	(29,878)	4,485	-	9,739	(29,878)
Changes in loss timing and other assumptions	(78,887)	61,411	(5,967)	-	(84,854)	61,411
Net (recoveries) losses and loss adjustment expenses	\$ (71,814)	\$ 35,317	\$ (623)	\$ -	\$ (72,437)	\$ 35,317
	2019	2018	2019	2018	2019	2018
Net (recoveries) losses and loss adjustment expenses	(71,814)	35,317	(623)	-	(72,437)	35,317
Losses and loss adjustment expenses paid or payable	(2,310)	(74,782)	-	-	(2,310)	(74,782)
Losses and loss adjustment expenses recovered or recoverable	-	301,407	(2,699)	-	(2,699)	301,407
Change in net liability	(74,124)	261,942	(3,322)	-	(77,446)	261,942
Net liability, beginning of period	217,908	252,312	120,011	-	337,919	252,312
Net liability, end of period	<u>\$ 143,784</u>	<u>\$ 514,254</u>	<u>\$ 116,689</u>	<u>\$ -</u>	<u>\$ 260,473</u>	<u>\$ 514,254</u>
Unpaid losses and loss adjustment expenses, end of period	\$ 312,508	\$ 643,785	\$ 116,689	\$ -	\$ 429,197	\$ 643,785
Salvage and subrogation recoverable, end of period	\$ 168,724	\$ 129,531	\$ -	\$ -	\$ 168,724	\$ 129,531

Note: Activity in the asset reinsurance recoverable on unpaid losses and loss adjustment expenses for ceded business mirrors the activity for the ceded business liability above.

Case Basis Reserves for Losses and Loss Adjustment Expenses

A summary of case basis reserves for losses and loss adjustment expenses as of March 31, 2019 and December 31, 2018 are as follows:

(U.S. dollars in thousands)	Retained business		Ceded business		Total	
March 31 and December 31,	2019	2018	2019	2018	2019	2018
HELOC, CES and Alt-A mortgage loan collateral	\$ 246,228	\$ 255,895	\$ 116,221	\$ 119,565	\$ 362,449	\$ 375,460
Public finance	64,911	108,592	468	446	65,379	109,038
CDOs	1,344	13	-	-	1,344	13
Structured single risk	25	1,274	-	-	25	1,274
Net unpaid losses and loss adjustment expenses, end of period	<u>\$ 312,508</u>	<u>\$ 365,774</u>	<u>\$ 116,689</u>	<u>\$ 120,011</u>	<u>\$ 429,197</u>	<u>\$ 485,785</u>

RMBS

Reserves for unpaid losses and loss adjustment expenses on the Company's guarantees of obligations supported by HELOC, CES and Alt-A mortgage loan collateral are determined based on an analysis of results of a cash flow model.

The cash flow model projects probability weighted average expected cash flows from the underlying mortgage notes. The model output is dependent on, and sensitive to, key input assumptions, including assumptions regarding default rates, draw rates, recoveries and prepayment rates. The cash flow from the mortgages is then run through the "waterfall" as set forth in the indenture for each transaction. Claims in respect of principal generally result when the outstanding principal balance of the mortgages is less than the outstanding principal balance of the insured notes. Recoveries result when cash flow from the mortgages is available for repayment, typically after the insured notes are paid off in full.

The Company bases its default assumptions for the second lien transactions (HELOCs and CESs) in large part on recent observed default rates and the current pipeline of delinquent loans. The losses for the second lien transactions (HELOCs and CESs) are estimated based on a model using a constant default rate curve.

The Company generally observed peak defaults for the second lien transactions in 2009 and 2010. Default rates at March 31, 2019 are mostly forecasted with steady state default rates. Exceptions to this may include transactions for which there is an excessive build-up of severely delinquent loans for which defaults are anticipated or transactions whose collateral includes loans whose interest-periods will end, at which point temporary increases to default rates are expected.

The Company assumes a steady state constant default rate taking into account historical performance. Net losses will be greater if default rates exceed the Company's current assumptions. The constant default rate is a function of several factors, one of which is the state of the economy and unemployment.

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The Company's default assumptions for the first lien transactions at March 31, 2019 and December 31, 2018 were based on current delinquent loans and analysis of historical defaults for loans with similar characteristics. A loss severity was applied to the first lien defaults ranging from 40% to 75% at March 31, 2019 and from 40% to 70% at December 31, 2018 based upon actual loss severity observances and collateral characteristics to determine the expected loss on the collateral in those transactions.

Schedule of Insured Financial Obligations with Credit Deterioration

The Company's surveillance department is responsible for monitoring the performance of its in-force portfolio. The surveillance department maintains a list of credits that it has determined need to be closely monitored and, for certain of those credits, the department undertakes remediation activities it determines to be appropriate in order to mitigate the likelihood and/or amount of any loss that could be incurred by the company with respect to such credits.

The surveillance department focuses its review on monitoring lower rated bond sectors and potentially troubled sectors, which have included certain subsectors within the RMBS, Public Finance and Structured Single Risk portfolios. For the RMBS portfolio, it tracks performance to determine whether or not covenants have been breached. If a covenant is breached, the Company may have the right to put the transaction into rapid amortization so that all cash flow generated from that transaction is used to pay down principal and stay current with interest or take other remedial action. Typically, the surveillance department reviews periodic servicing and trustee reports to track coverage levels, enhancement levels, delinquency levels, loss frequency, loss severity and total losses and compares such performance metrics with the metrics that were made available at the time the transaction was closed. If losses are above projections, the surveillance department will analyze the reasons for the deviation. In some cases, it may be an indication of servicing problems, where loans are delinquent and are not put into foreclosure in time to maximize recovery.

The Company estimates claims based on its surveillance department's best estimate of net cash outflows under a contract, on a present value basis. In some cases, the surveillance department will engage an outside consultant with appropriate expertise in the underlying collateral assets and respective industries to assist management in examining the underlying collateral and determining the projected loss frequency and loss severity. In such cases, the surveillance department will use that information to run a cash flow model that includes enhancement levels and debt service to determine whether a claim is probable, possible or not likely.

The activities of the Company's surveillance department are integral to the identification of specific credits that have experienced deterioration in credit quality and the assessment of whether losses on such credits are probable, as well as any estimation of the amount of loss expected to be incurred with respect to such credits. Closely monitored credits are divided into four categories: (i) Loss List—credits where a loss is probable and reasonably estimable; (ii) Red Flag List—credits where a loss is possible but not probable or reasonably estimable, including credits where claims may have been paid or may be paid but full recovery is in doubt; (iii) Yellow Flag List—credits that the Company determines to be non-investment grade but a loss is unlikely, including credits where claims may have been paid or may be paid but reimbursement is likely; and (iv) Special Monitoring List—low investment grade credits where a material covenant or trigger may be breached and closer monitoring is warranted. Credits that are not closely monitored credits are considered to be fundamentally sound, normal risk.

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The following tables set forth certain information in regard to the Company's closely monitored credits as of March 31, 2019 and December 31, 2018, respectively. The number of policies, remaining weighted-average contract period, and insured contractual payments outstanding in the table below excludes exposures that were effectively defeased or, in-substance, commuted through the acquisition of Insurance Cash Flow Certificates and related alternative structures, but includes those ceded to Assured.

(U.S. dollars in millions)	Loss List		Red Flag List		Yellow Flag List		Special Monitoring List	
	2019	2018	2019	2018	2019	2018	2019	2018
Retained business								
Insured contractual payments outstanding:								
Principal	\$ 186	\$ 186	\$ 15	\$ 15	\$ 256	\$ 254	\$ 126	\$ 130
Interest	61	64	9	9	101	103	58	60
Total	<u>\$ 247</u>	<u>\$ 250</u>	<u>\$ 24</u>	<u>\$ 24</u>	<u>\$ 357</u>	<u>\$ 357</u>	<u>\$ 184</u>	<u>\$ 190</u>
Number of policies	63	64	1	1	1	1	1	1
Remaining weighted-average contract period (in years)	<u>6.7</u>	<u>7.0</u>	<u>13.2</u>	<u>13.4</u>	<u>15.0</u>	<u>15.1</u>	<u>16.7</u>	<u>16.9</u>
Unpaid loss and loss adjustment expenses:								
Gross amount before reductions	\$ 641	\$ 809	\$ 3	\$ 3	\$ 7	\$ 6	\$ -	\$ -
Gross estimated recoveries	(222)	(298)	-	-	(1)	(2)	-	-
Unearned premium revenue ⁽¹⁾	(9)	(9)	-	-	(2)	-	-	-
Present value discount	(104)	(143)	-	-	-	-	-	-
Total	<u>\$ 306</u>	<u>\$ 359</u>	<u>\$ 3</u>	<u>\$ 3</u>	<u>\$ 4</u>	<u>\$ 4</u>	<u>\$ -</u>	<u>\$ -</u>
Ceded business								
Insured contractual payments outstanding:								
Principal	\$ 268	\$ 271	\$ 6	\$ 6	\$ 184	\$ 184	\$ 269	\$ 268
Interest	94	95	-	1	143	144	20	20
Total	<u>\$ 362</u>	<u>\$ 366</u>	<u>\$ 6</u>	<u>\$ 7</u>	<u>\$ 327</u>	<u>\$ 328</u>	<u>\$ 289</u>	<u>\$ 288</u>
Number of policies	11	11	1	1	8	8	6	6
Remaining weighted-average contract period (in years)	<u>13.0</u>	<u>13.1</u>	<u>3.5</u>	<u>3.3</u>	<u>15.1</u>	<u>15.2</u>	<u>4.5</u>	<u>4.8</u>
Unpaid loss and loss adjustment expenses:								
Gross amount before reductions	\$ 176	\$ 187	\$ -	\$ -	\$ 1	\$ -	\$ -	\$ -
Gross estimated recoveries	-	-	-	-	-	-	-	-
Unearned premium revenue ⁽¹⁾	(3)	(3)	-	-	-	-	-	-
Present value discount	(57)	(64)	-	-	-	-	-	-
Total	<u>\$ 116</u>	<u>\$ 120</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

⁽¹⁾ The claim liability is determined on a contract by contract basis. As such, instances may arise where the unearned premium revenue on a contract may exceed the present value of the expected net cash outflows. The unearned premium in the table above represents the aggregate of unearned premium revenue on each contract but not in excess of the associated present value of the expected net cash outflows on such contract.

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Credit Default Swap Contracts

Credit default swap contracts are derivative financial instruments and are recorded at fair value. Changes in fair value are recorded in "net (loss) earnings on credit default and other swap contracts" on the consolidated statements of operations. Realized gains (losses) and other settlements on credit default swap contracts include credit default swap derivative premiums received and receivable for credit protection the Company has sold under its insured CDS contracts, contractual claims paid and payable and received and receivable related to insured credit events under these contracts, ceding commissions expense or income and realized gains or losses related to their early termination. Net unrealized gains (losses) on credit default swaps contracts represent the adjustments for changes in fair value in excess of realized gains and other settlements that are recorded in each reporting period. Fair value of credit default swap contracts is reflected as either net assets or net liabilities determined on a contract by contract basis in the Company's consolidated balance sheets. See Note 11 for a discussion on the fair value methodology for credit default swap contracts.

Credit Default and Other Swap Contract Liabilities

CDS contracts are derivative contracts which offer credit protection relating to a particular security or pools of securities, which are specifically referenced in the CDS contract. Under the terms of a CDS contract, the seller of credit protection (the issuer of the CDS contract) makes a specified payment to the buyer of such protection (the CDS contract counterparty) upon the occurrence of one or more credit events specified in the CDS contract with respect to a referenced security or securities. The terms of the CDS contracts issued by the Company generally only require the Company to make a payment upon the occurrence of one or more specified credit events after exhaustion of various levels of subordination or first-loss protection. In addition, pursuant to the terms of the Company's CDS contracts, the Company is precluded from transferring such contracts to other market participants without the consent of the counterparty.

Securities or assets referenced in the Company's in-force CDS contracts primarily include structured pools of obligations, such as collateralized loan obligations, corporate CDOs and CMBS CDOs. Such pools were rated investment-grade or better at the issuance of the CDS contract.

Typical market CDS contracts are standardized, liquid instruments that reference tradable securities such as corporate bonds. These market standard CDS contracts also involve collateral posting, and upon a default of the referenced obligation, can be settled in cash. In contrast, the Company's CDS contracts do not contain the typical CDS market standard features as described above but have been customized to replicate the Company's financial guarantee insurance. The Company's CDS contracts provide protection on specified obligations, such as those described above and, generally, contain some form of subordination prior to the attachment of the Company's liability. The Company is not required to post collateral and, upon an underlying default, the Company generally makes payments on a "pay-as-you-go" basis after the subordination in a transaction is exhausted.

The Company's payment obligations after a default vary by deal type. There are three primary types of policy payment requirements: timely interest and ultimate principal, ultimate principal only at final maturity and payments upon settlement of individual collateral losses as they occur upon erosion of subordination.

The Company's CDS contracts are generally governed by a single transaction International Swaps and Dealers Association Master Agreement relating only to that particular transaction/contract. Under most monoline financial guarantee standard termination provisions, there is no requirement for mark-to-market termination payments upon the early termination of a guaranteed CDS contract. However, substantially all of the Company's CDS contracts provided for mark-to-market termination payments following the occurrence of events that are outside the Company's control, such as SGI being placed into receivership or rehabilitation or a regulator taking control of SGI or, in some instances, SGI's insolvency. Pursuant to the 2009 MTA, substantially all of the Company's guarantees of CDS contracts that were not commuted were novated to SCAI (pre-merger in 2017) and amended to remove any events triggering mark-to-market termination payments except for SCAI (pre-merger in 2017) failing to make payment under the applicable contract or being placed into receivership or rehabilitation or a regulator taking control of SCAI (pre-merger in 2017). Under current market conditions, if the Company were required to pay such termination payments, it may result in a liability to the Company which may be in excess of that currently recorded by the Company. An additional difference between the Company's CDS contracts and the typical market standard CDS contracts is that, except in the circumstances noted above, there is no acceleration of the payment to be made under the Company's CDS contracts unless the Company, at its option, elects to accelerate. Furthermore, by law, the Company's guarantees are unconditional and irrevocable, and cannot be transferred to most other capital market participants as they are not licensed to write such business. However, through the purchase of back-to-back credit protection, the risk of loss (but not counterparty risk) on these contracts can be transferred to other financial guarantee insurance and reinsurance companies.

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Credit Default and Other Swap Contract Assets

In connection with the Company's reinsurance agreement with Assured, substantially all of the CDS contracts insured by the Company have been reinsured by Assured. These CDS contracts are recorded at fair value and do not qualify for reinsurance accounting treatment. As a result, the Company recorded credit default and other swap contracts assets, which represent the fair value of the reinsurance of these CDS contracts, which will offset the Company's credit default swap and other swap contract liabilities recorded on the consolidated balance sheets. Since the fair value of these CDS assets and CDS liabilities will be equal, any subsequent changes to the fair value of these reinsured CDS contracts will result in the equal offset to the CDS liabilities and corresponding CDS assets on the consolidated balance sheets.

The following tables provide the components of net (loss) earnings on credit default and other swap contracts for the three months ended March 31, 2019 and 2018 and certain information regarding the Company's in-force CDS and other swap contracts as of March 31, 2019 and December 31, 2018, including the aggregate notional amount outstanding, the weighted average life of such contracts, and the ratings of obligations referenced in such contracts.

(U.S. dollars in thousands)	Retained business		Ceded business		Total	
	2019	2018	2019	2018	2019	2018
Three months ended March 31,						
Contract premiums earned	\$ 69	\$ 799	\$ -	\$ -	\$ 69	\$ 799
Net unrealized gains (losses) on contract liabilities	(1,947)	(21,903)	446	-	(1,501)	(21,903)
Net unrealized gains (losses) on contract assets	-	-	(446)	-	(446)	-
Net (loss) earnings on credit default and other swap contracts ⁽¹⁾	\$ (1,878)	\$ (21,104)	\$ -	\$ -	\$ (1,878)	\$ (21,104)
	2019	2018	2019	2018	2019	2018
Net loss (earnings) on credit default and other swap contracts	\$ 1,878	\$ 21,104	\$ (446)	\$ -	\$ 1,432	\$ 21,104
Other	482	1,016	(402)	-	80	1,016
Change in credit default swaps and other swap contract liabilities	2,360	22,120	(848)	-	1,512	22,120
Credit default swaps and other swap contract liabilities, beginning of period	8,489	104,094	227,052	-	235,541	104,094
Credit default swaps and other swap contract liabilities, end of period	\$ 10,849	\$ 126,214	\$ 226,204	\$ -	\$ 237,053	\$ 126,214
	2019	2018	2019	2018	2019	2018
March 31 and December 31,						
Fair value of credit default and other swap contracts	\$ 10,849	\$ 8,489	\$ 226,204	\$ 227,052	\$ 237,053	\$ 235,541
Notional amount outstanding	\$ 145,857	\$ 145,857	\$3,014,774	\$2,978,319	\$3,160,631	\$3,124,176
Weighted average life (years)	20.1	20.3	21.8	21.9	21.8	21.9
Percentage of referenced assets by rating ⁽²⁾						
AAA	-	-	7.7%	7.6%		
At or above investment grade but below AAA	100.0%	100.0%	92.3%	92.4%		
Below investment grade	-	-	-	-		
Total	100.0%	100.0%	100.0%	100.0%		
Liability fair value before giving effect to non-performance risk	\$ 16,146	\$ 14,385	\$ 277,282	\$ 294,019	\$ 293,428	\$ 308,404
Non-performance risk	(5,297)	(5,896)	(51,078)	(66,967)	(56,375)	(72,863)
Fair value of liabilities, as above	\$ 10,849	\$ 8,489	\$ 226,204	\$ 227,052	\$ 237,053	\$ 235,541

⁽¹⁾ The change in net realized/unrealized gains (losses) relating to the CDS and other swap contracts still held as of March 31, 2019 and 2018 was \$(1.9) million and \$(21.1) million, respectively.

⁽²⁾ Based on S&P rating as reflected in Syncora's records, if available, and internal Syncora's rating if no S&P rating is available.

Note: Activity in the asset credit default and other swap contracts for ceded business mirrors the activity for the ceded business liability above.

Consolidation of VIEs

The Company has exposure to VIEs primarily through the issuance of financial guaranty insurance contracts that typically insure the timely payment of principal and interest with respect to debt obligations of the VIEs. As part of the terms of its insurance contracts, at the outset of a contract, the Company obtains certain protective rights with respect to the VIE that are triggered by the occurrence of certain events, such as failure to be in compliance with a covenant due to poor deal performance or a deterioration in a servicer or collateral manager's financial condition. At deal inception, the Company typically is not deemed to control a VIE; however, once a trigger event occurs, the Company's control of the VIE typically increases. In addition, the Company has exposure to VIEs through the ownership of Uninsured Cash Flow Certificates ("UCFs") and other interests from its remediation transactions.

The Company is not primarily liable for the debt obligations issued by the VIEs; however, where the Company has issued an insurance contract, the Company would only be required to make payments on the debt obligations in the event that the issuer of such debt obligations defaults on any principal or interest due. The Company or the Company's creditors do not have any rights with regard to the assets of the VIEs.

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The following table presents the revenues and expenses and a rollforward of fair value of consolidated VIEs included in the Company's consolidated balance sheets and statements of operations as of March 31, 2019 and 2018 and for the three months ended March 31, 2019 and 2018. In addition, the table presents the fair value of the consolidated VIE assets and liabilities of the retained business only in the Company's consolidated balance sheets, segregated by the types of assets held by VIEs that collateralize their respective debt obligations as of March 31, 2019 and December 31, 2018. As of March 31, 2019 and December 31, 2018, the Company's qualitative and quantitative analyses have indicated that it does not have a controlling financial interest in any other VIEs.

(U.S. dollars in thousands)	Retained business	
Three months ended March 31,	2019	2018
Investment income	\$ 1,468	\$ 19,116
Interest and other expenses	(37)	(2,665)
Net realized and unrealized (losses) gains	(1,141)	(14,581)
Net change in fair value of consolidated variable interest entities	290	1,870
Distribution of investment income, net of interest and other expenses	(1,431)	(16,450)
Other distributions from variable interest entities	(271)	(32,795)
Paydowns of liabilities	-	8,340
Net change in consolidated variable interest entities' net assets	(1,412)	(39,035)
Consolidated variable interest entities' net assets, beginning of period	20,503	57,446
Net assets of consolidated variable interest entities, end of period	\$ 19,091	\$ 18,411

March 31 and December 31,	Net Assets		Assets		Liabilities	
	2019	2018	2019	2018	2019	2018
Subprime (1st lien)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Prime (HELOC)	11,953	13,456	12,229	13,770	276	314
Alt-A (2nd lien)	6,075	6,291	6,075	6,291	-	-
Alt-A (1st lien)	1,063	756	1,103	782	40	26
	\$ 19,091	\$ 20,503	\$ 19,407	\$ 20,843	\$ 316	\$ 340

The Company's maximum exposure to loss provided through its financial guarantees of principal and interest with respect to debt obligations of unconsolidated variable interest entities was \$670.0 million (includes principal of \$495.9 million and interest of \$174.1 million) and \$682.3 million (includes principal of \$502.8 and interest of \$179.5 million) at March 31, 2019 and December 31, 2018, respectively. The Company's retained business net principal outstanding was \$925 million and 933 million as of March 31, 2019 and December 31, 2018, respectively.

Exposures Under Guarantees

While the Company establishes reserves for losses and loss adjustment expenses on obligations it has guaranteed or reinsured, the risk of loss under the Company's guarantees extends to the full amount of unpaid principal and interest on all debt obligations it has guaranteed. Set forth below are tables which reflect certain information regarding the Company's in-force principal and interest exposure at March 31, 2019 and December 31, 2018.

SYNCORA HOLDINGS LTD.
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The following table sets forth the Company's in-force guaranteed principal by bond sector as of March 31, 2019 and December 31, 2018, respectively:

Bond Exposure
(U.S. dollars in millions)

	Retained business		Ceded business		Total	
	2019	2018	2019	2018	2019	2018
Public Finance						
Special Revenue	\$ 233	\$ 237	\$ 2,692	\$ 2,748	\$ 2,925	\$ 2,985
General Obligation	106	106	944	969	1,050	1,075
Utility	82	82	585	611	667	693
Non Ad Valorem	7	7	503	513	510	520
Other	3	3	-	-	3	3
Appropriation	-	-	301	302	301	302
Total Public Finance	\$ 431	\$ 435	\$ 5,025	\$ 5,143	\$ 5,456	\$ 5,578
Asset-Backed Securities						
RMBS	\$ 1	\$ 1	\$ 319	\$ 323	\$ 320	\$ 324
Total Asset-Backed Securities	\$ 1	\$ 1	\$ 319	\$ 323	\$ 320	\$ 324
Collateralized Debt Obligations						
Cashflow CDO	\$ 2	\$ 2	\$ 14	\$ 15	\$ 16	\$ 17
Total Collateralized Debt Obligations	\$ 2	\$ 2	\$ 14	\$ 15	\$ 16	\$ 17
Structured Single Risk						
Global Infrastructure	\$ 365	\$ 365	\$ 1,858	\$ 1,850	\$ 2,223	\$ 2,215
Specialized Risk	126	130	50	50	176	180
Power & Utilities	-	-	3,642	3,565	3,642	3,565
Total Structured Single Risk	\$ 491	\$ 495	\$ 5,550	\$ 5,465	\$ 6,041	\$ 5,960
Total Outstanding	\$ 925	\$ 933	\$ 10,908	\$ 10,946	\$ 11,833	\$ 11,879

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The following table sets forth the number of years to maturity of the Company's in-force guaranteed principal and interest exposure at March 31, 2019:

Years to Maturity - Debt Service Amortization
(U.S. dollars in millions)

	Retained business		Ceded Business		Total	
	Scheduled Net Debt Amortization	Principal and Interest Outstanding	Scheduled Net Debt Amortization	Principal and Interest Outstanding	Scheduled Net Debt Amortization	Principal and Interest Outstanding
2019 Q1	\$ -	\$ 1,412	\$ -	\$ 17,412	\$ -	\$ 18,824
2019 Q2	6	1,406	123	17,289	129	18,695
2019 Q3	29	1,377	217	17,072	246	18,449
2019 Q4	28	1,349	162	16,910	190	18,259
Total 2019	\$ 63		\$ 502		\$ 565	
2020	\$ 69	\$ 1,280	\$ 827	\$ 16,083	\$ 896	\$ 17,363
2021	75	1,205	1,080	15,003	1,155	16,208
2022	68	1,137	781	14,222	849	15,359
2023	87	1,050	616	13,606	703	14,656
Total 2020-2023	\$ 299		\$ 3,304		\$ 3,603	
2024-2028	\$ 397	\$ 653	\$ 3,366	\$ 10,240	\$ 3,763	\$ 10,893
2029-2033	209	444	1,862	8,378	2,071	8,822
2034-2038	189	255	2,015	6,363	2,204	6,618
2039 and thereafter	255	-	6,363	-	6,618	-
Total 2024-thereafter	\$ 1,050		\$ 13,606		\$ 14,656	
Total	\$ 1,412		\$ 17,412		\$ 18,824	

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The following table sets forth the Company's in-force guaranteed principal exposure by geographic concentration at March 31, 2019 and December 31, 2018, respectively:

Geographic Distribution - Par Exposure
(U.S. dollars in millions)

	Retained business				Ceded business			
	Amount		%		Amount		%	
	2019	2018	2019	2018	2019	2018	2019	2018
United States								
Puerto Rico	\$ 180	\$ 180	19.4 %	19.3 %	\$ -	\$ -	-	-
Multi-state ⁽¹⁾⁽²⁾	148	148	16.2	16.0	316	320	2.9	2.9
New York	88	92	9.5	9.8	615	612	5.6	5.6
California	15	15	1.6	1.6	1,956	2,000	18.1	18.4
Michigan	3	3	0.3	0.3	21	22	0.2	0.2
Virginia	-	-	-	-	596	596	5.5	5.4
Other ⁽³⁾	-	-	-	-	593	642	5.4	5.9
District Of Columbia	-	-	-	-	412	416	3.8	3.8
Florida	-	-	-	-	223	223	2.0	2.0
Georgia	-	-	-	-	220	240	2.0	2.2
Washington	-	-	-	-	201	201	1.8	1.8
Massachusetts	-	-	-	-	169	169	1.5	1.5
Missouri	-	-	-	-	168	169	1.5	1.5
New Jersey	-	-	-	-	161	161	1.5	1.5
Nebraska	-	-	-	-	130	131	1.2	1.2
Ohio	-	-	-	-	129	130	1.2	1.2
Oregon	-	-	-	-	123	125	1.1	1.1
Total United States	\$ 434	\$ 438	47.0 %	47.0 %	\$ 6,033	\$ 6,157	55.3 %	56.2 %
International								
United Kingdom	\$ 257	\$ 254	27.6 %	27.3 %	\$ 3,903	\$ 3,813	35.9 %	34.8 %
Italy	126	130	13.7	13.9	-	-	-	-
Portugal	108	111	11.7	11.8	-	-	-	-
New Zealand	-	-	-	-	310	306	2.8	2.8
Chile	-	-	-	-	264	272	2.4	2.5
Australia	-	-	-	-	234	233	2.1	2.1
Canada	-	-	-	-	98	98	0.9	0.9
Mexico	-	-	-	-	50	50	0.5	0.5
Panama	-	-	-	-	16	17	0.1	0.2
Total International	\$ 491	\$ 495	53.0 %	53.0 %	\$ 4,875	\$ 4,789	44.7 %	43.8 %
Total Par Outstanding	\$ 925	\$ 933	100.0 %	100.0 %	\$ 10,908	\$ 10,946	100.0 %	100.0 %

⁽¹⁾ Deals with underlying securities in multiple states.

⁽²⁾ Consists of \$145 million and \$145 million of Public Finance net par in 2019 and 2018, respectively, \$2 million and \$2 million of CDO net par in 2019 and 2018, respectively, and \$1 million and \$1 million of ABS net par in 2019 and 2018, respectively.

⁽³⁾ Single state with par outstanding < 1% of the total exposure in the current period.

Effective Commutation or Defeasance of Syncora Guarantee's Exposure to Insured RMBS Securities (the "RMBS Offer")

In connection with the 2009 MTA, the Company invested in a fund (the "RMBS Fund") that executed certain transactions designed to effectively defease or, in-substance, commute the Company's exposure on certain of its financial guarantee insurance policies written on RMBS. The RMBS Fund purchased certain of such RMBS in return for a trust certificate of an owner trust representing the uninsured cash flows of such RMBS UCFs plus a cash payment. In general, the RMBS Fund contributed any such purchased RMBS (and certain of the Company's reimbursement rights) to separate owner trusts in return for certificates representing the cash flows consisting of insurance payments made on the policies insuring such RMBS ("Insurance Cash Flow Certificates"). In return for such investments, the Insurance Cash Flow Certificates were distributed to the Company. The Company will, should the cash flows from the underlying RMBS transaction be sufficient, receive certain reimbursement payments in respect of insurance payments previously made by the Company on such RMBS. The Company also entered into several alternative transactions effectively replicating the economics of the RMBS Offer.

In addition to the RMBS Offer, the Company directly purchased certain RMBS and other securities that it had insured. Certain of these directly purchased securities were exchanged by the Company for Insurance Cash Flow Certificates and Uninsured

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Cash Flow Certificates using the mechanics described above. The Uninsured Cash Flow Certificate may either be held or resold by the Company. In connection with the reinsurance transaction as discussed above, the Company has substantially ceded all of its RMBS exposure to Assured.

As the Insurance Cash Flow Certificates do not legally extinguish the RMBS or other insured securities, the Company regards the effective purchase of the Insurance Cash Flow Certificates as providing protection on the underlying securities upon the occurrence of an event of default and consequently follows reinsurance accounting principles. Upon the indirect or direct purchase of insured securities a deferred gain is recorded that represents the excess of the estimated ultimate claim payments relating to the insured securities at the time of the transaction over the cost the Company paid for those Insurance Cash Flow Certificates. The deferred gain is recognized in the consolidated statements of operations in “Net (loss) earnings on insurance cash flow certificates” based on the anticipated claim payments at the time of the transaction. The assumptions used in estimating the receivables on the Insurance Cash Flow Certificates for any given period are recognized in a manner consistent with the measurement and recognition of the loss reserves associated with the insured securities.

The following table presents the activity in the Company’s receivables on insurance cash flow certificates, net of deferred gains for the three months ended March 31, 2019 and 2018:

(U.S. dollars in thousands) Three months ended March 31,	Retained business	
	2019	2018
Amortization of deferred gains	\$ 683	\$ 615
Change in estimated cash flows underlying anticipated claim payments	(14,411)	33,718
Net (loss) earnings on insurance cash flow certificates	(13,728)	34,333
Cash paid for insurance cash flow certificates	-	77
Cash received on insurance cash flow certificates	-	(1,133)
Settlements	(223)	(64)
Change in receivables on insurance cash flow certificates	(13,951)	33,213
Receivables on insurance cash flow certificates, beginning of period	91,905	109,869
Receivables on insurance cash flow certificates, end of period	\$ 77,954	\$ 143,082

Exposure to RMBS

The following table presents the net principal outstanding for the Company’s insured RMBS portfolio by type of collateral⁽¹⁾ as of March 31, 2019 and December 31, 2018, respectively:

RMBS Exposure
(U.S. dollars in millions)

	Retained business				Ceded business			
	Amount		%		Amount		%	
	2019	2018	2019	2018	2019	2018	2019	2018
Prime (1st lien)	\$ -	\$ -	-	-	\$ 14	\$ 14	4.4 %	4.4 %
Prime (2nd lien)	-	-	-	-	4	5	1.4	1.5
Prime (HELOC)	1	1	100.0	100.0	50	51	15.5	15.9
Alt-A (1st lien)	-	-	-	-	19	20	6.1	6.1
Alt-A (2nd lien)	-	-	-	-	1	2	0.4	0.5
Subprime (1st lien)	-	-	-	-	211	210	65.8	65.2
Subprime (2nd lien)	-	-	-	-	4	4	1.4	1.2
Subprime (1st lien) - International	-	-	-	-	16	17	5.0	5.2
Total RMBS Outstanding	\$ 1	\$ 1	100.0 %	100.0 %	\$ 319	\$ 323	100.0 %	100.0 %

⁽¹⁾ Collateral type is defined as follows: Prime (1st lien) mortgage loans are secured by first liens on one-to-four family residential properties. The underwriting standards used to underwrite prime mortgage loans are the standards applied to the most creditworthy borrowers and are generally acceptable to Fannie Mae and Freddie Mac. Prime (2nd lien) mortgage loans are secured by 2nd liens on one-to-four family residential properties. The underwriting standards used to underwrite prime mortgage loans are the standards applied to the most creditworthy borrowers and are generally acceptable to Fannie Mae and Freddie Mac. This category also includes Alt-A (2nd lien) loans. HELOC is an adjustable rate line of credit secured by a second lien on residential properties. An Alt-A loan means a mortgage loan secured by first liens on residential properties, which is ineligible for purchase by Fannie Mae or Freddie Mac. Subprime (1st lien) mortgage loans are secured by first liens on residential properties to non-prime borrowers. The underwriting standards used to underwrite subprime mortgage loans are less stringent than the standards applied to the most creditworthy borrowers and less stringent than the standards generally acceptable to Fannie Mae and Freddie Mac with regard to the borrower’s credit standing and repayment ability. Subprime (2nd lien) mortgage loans are secured by second liens on residential properties to non-prime borrowers. See Subprime (1st lien) for a description of the underwriting standards. Subprime (1st lien) – International mortgage loans are secured by first liens on residential properties to non-prime borrowers located outside the United States.

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6. Investments and Cash

Investments

The Company determines the appropriate classification of investments at the time of purchase, which are recorded on the trade date. All of the Company's investments in debt (including UCFs) and equity securities are considered available-for-sale and accordingly are reported at fair value. The fair value of investments is based on quoted market prices received from nationally recognized pricing services or, in the absence of quoted market prices, dealer quotes or determined using the Company's own internal model estimates. Net unrealized gains or losses on debt securities, net of deferred income taxes, are included in accumulated other comprehensive income. Effective January 1, 2018, net unrealized gains or losses on equity investments are included in the consolidated statement of operations and comprehensive loss. Any unrealized loss in value on debt securities considered by management to be other-than-temporary is charged to income in the period that such determination is made.

Bond discounts and premiums are amortized on a level-yield basis over the remaining terms of securities acquired. For pre-refunded bonds, the remaining term is determined based on the contractual refunding date. For mortgage-backed securities, and any other holdings for which prepayment risk may be significant, assumptions regarding prepayments are evaluated periodically and revised as necessary. Any adjustments required due to the resulting change in effective yields are recognized in income in the period such change is made.

Cash and Cash Equivalents

The Company's cash and cash equivalents include cash on hand, interest bearing bank deposits, commercial paper and money market funds. The Company defines cash equivalents as short-term, highly liquid securities and interest earning deposits with maturities at time of purchase of 90 days or less.

Restricted Cash and Cash Equivalents

Restricted cash and cash equivalents are restricted as to withdrawal and use by the Company. Restricted cash and cash equivalents primarily include deposits held in escrow accounts and cash deposits or allowable funds held to satisfy regulatory requirements.

The amortized cost and fair value of investments as of March 31, 2019 and December 31, 2018 are as follows:

(U.S. dollars in thousands)	Cost or		Gross Unrealized		Gross Unrealized		Fair Value	
	Amortized Cost		Gains		Losses			
	<u>2019</u>	<u>2018</u>	<u>2019</u>	<u>2018</u>	<u>2019</u>	<u>2018</u>	<u>2019</u>	<u>2018</u>
Debt securities								
Mortgage-backed securities:								
RMBS ⁽¹⁾	\$ 76,036	\$ 70,224	\$ 2,854	\$ 1,951	\$ (25)	\$ (137)	\$ 78,865	\$ 72,038
CMBS.....	37,929	29,805	359	70	(599)	(702)	37,689	29,173
Asset-backed securities.....	77,697	67,893	539	153	(2,447)	(2,942)	75,789	65,104
U.S. Government and government agencies.....	63,135	95,406	538	236	(1)	(28)	63,672	95,614
Corporate and Other.....	333,104	318,523	5,185	779	(282)	(3,033)	338,007	316,268
U.S. states and political subdivisions of the states....	29,604	31,316	4,132	3,981	(3)	(7)	33,733	35,291
Total debt securities.....	<u>\$ 617,505</u>	<u>\$ 613,167</u>	<u>\$ 13,607</u>	<u>\$ 7,170</u>	<u>\$ (3,357)</u>	<u>\$ (6,849)</u>	<u>\$ 627,755</u>	<u>\$ 613,488</u>
Total other invested assets ⁽²⁾	<u>\$ 91,502</u>	<u>\$ 91,364</u>	<u>\$ 5,958</u>	<u>\$ 2,368</u>	<u>\$ (2,819)</u>	<u>\$ (6,228)</u>	<u>\$ 94,641</u>	<u>\$ 87,504</u>

⁽¹⁾ At March 31, 2019, residential mortgage-backed securities include \$1.4 million of fair value and \$0.2 million of amortized cost related to UCFs. At December 31, 2018, residential mortgage-backed securities include \$1.5 million of fair value and \$0.1 million of amortized cost related to UCFs.

⁽²⁾ At March 31, 2019 and December 31, 2018, other invested assets, which consist of common stock and private equity investments, include \$(1.4) million and \$(8.4) million, respectively, of net unrealized gains (losses) that were recorded through net income on the consolidated statement of operations on investments in which the Company has elected the fair value option.

The change in net unrealized gains (losses) consists of changes in the valuation and holdings of debt securities of \$9.9 million and \$(8.3) million for the three months ended March 31, 2019 and 2018, respectively.

Proceeds from sales of debt securities, net of receivables, for the three months ended March 31, 2019 and 2018 were \$45.1 million and \$64.6 million, respectively.

The gross realized and unrealized gains and gross realized and unrealized (losses) recognized in income, excluding other-than-temporary impairment losses, for the three months ended March 31, 2019 and 2018 were \$7.8 million and \$14.4 million and \$(0.6) million and \$(2.5) million, respectively. Realized investment gains and losses on the sale of investments are determined on the basis of the first-in first-out method and are included in net income.

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The amortized cost and fair value of bonds at March 31, 2019 and December 31, 2018 by contractual maturity are shown below. Actual maturity may differ from contractual maturity because issuers may have the right to call or prepay obligations with or without call or prepayment penalties. Mortgage-backed securities are generally more likely to be prepaid than other fixed-maturity securities. As the stated maturities of such securities may not be indicative of actual maturities, the totals for mortgage-backed securities are shown separately.

	2019		2018	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
(U.S. dollars in thousands)				
Due within one year	\$ 33,154	\$ 33,218	\$ 38,457	\$ 38,411
Due after one through five years	295,235	298,487	317,855	316,795
Due after five through ten years	85,754	90,576	71,745	73,497
Due after ten years	11,700	13,131	17,188	18,470
Subtotal	425,843	435,412	445,245	447,172
Mortgage- and asset-backed securities	191,662	192,343	167,922	166,316
Total	\$ 617,505	\$ 627,755	\$ 613,167	\$ 613,488

Net investment income for the three months ended March 31, 2019 and 2018 is derived from the following sources:

(U.S. dollars in thousands)	2019	2018
Debt securities and cash and cash equivalents	\$ 7,162	\$ 9,353
Equity securities	1,472	1,107
Other invested assets	176	244
Less: Investment expenses	(221)	(323)
Net investment income	\$ 8,589	\$ 10,381

The Company has a formal review process for all debt securities in the Company's investment portfolio, including a review for impairment losses. Factors considered when assessing impairment include: a decline in the market value of a security by 20% or more below amortized cost for a continuous period of at least six months; a decline in the market value of a security for a continuous period of 12 months; recent credit downgrades of the applicable security or the issuer by rating agencies; the financial condition of the applicable issuer; whether loss of investment principal is anticipated; whether scheduled interest payments are past due; and whether the Company intends to sell the security prior to its recovery in fair value.

The Company's review process, in certain instances, also includes analyses of the ability to recover the amortized cost by comparing the net present value of projected future cash flows with the amortized cost of the security. If the Company believes a decline in the value of a particular investment is temporary, the Company records the decline as an unrealized loss on the Company's consolidated balance sheets in "accumulated other comprehensive income" in shareholders' equity. The Company recognizes an other-than-temporary impairment loss in the consolidated statements of operations for a debt security in an unrealized loss position when either the Company has the intent to sell the debt security or it is more-likely-than not that the Company will be required to sell the debt security before its anticipated recovery.

Any credit-related impairment on debt securities the Company does not plan to sell and more-likely-than-not will not be required to sell is recognized in the consolidated statement of operations, with the non-credit-related impairment recognized in other comprehensive income. For other impaired debt securities, where the Company has the intent to sell the security or where the Company will more-likely-than not be required to sell or where the entire impairment is deemed by the Company to be credit-related, the entire impairment is recognized in the consolidated statements of operations.

If it is determined that an impairment is other than temporary, then an impairment loss is recognized in the consolidated statements of operations equal to the difference between the investment's amortized cost and its fair value at the balance sheet date for which the assessment is made. The measurement of the impairment shall not include partial recoveries after the balance sheet date. The fair value of the investment becomes the new cost basis of the investment and shall not be adjusted for subsequent recoveries in fair value.

The Company's assessment of a decline in value includes management's current assessment of the factors noted above. If that assessment changes in the future, the Company may ultimately record a loss after having originally concluded that the decline in value was temporary.

For the three months ended March 31, 2019 and 2018, the Company recorded other-than-temporary impairment charges of \$0.3 million and \$10.9 million, respectively, on its debt securities. The other-than-temporary impairment charges recorded by the Company during the three months ended March 31, 2019 were primarily due to the present value of projected cash flows expected to be collected being less than the carrying value of the securities. The other-than-temporary impairment charges recorded by the

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Company during the three months ended March 31, 2018 were primarily due to foreign currency exchange losses on certain debt securities and the Company's conclusion, resulting from its near term anticipated cash needs, that it was more-likely-than not that the Company would be required to sell certain debt securities (including its UCFs) before recovering their cost.

The following tables present the aggregate gross unrealized losses and fair value by investment category at March 31, 2019 and December 31, 2018, respectively. There were no securities in a gross unrealized loss position for greater than 12 months at December 31, 2018.

(U.S. dollars in thousands)

<u>Less than 12 Months</u>	<u>Unrealized loss</u>		<u>Fair value</u>		<u>Number of securities</u>	
	<u>2019</u>	<u>2018</u>	<u>2019</u>	<u>2018</u>	<u>2019</u>	<u>2018</u>
Mortgage-backed securities:						
RMBS.....	\$ (25)	\$ (137)	\$ 5,851	\$ 53,046	9	50
CMBS.....	(325)	(702)	7,613	25,940	8	37
Asset-backed securities.....	(2,444)	(2,942)	22,534	34,099	13	24
US Government and government agency..	(1)	(28)	2,470	63,293	4	16
Corporate and other.....	(52)	(3,033)	6,275	256,667	10	248
US states & political subdivisions.....	(3)	(7)	402	2,243	1	3
Total debt securities.....	<u>\$ (2,850)</u>	<u>\$ (6,849)</u>	<u>\$ 45,145</u>	<u>\$ 435,288</u>	<u>45</u>	<u>378</u>
Total other invested assets.....	<u>\$ (2,679)</u>	<u>\$ (6,228)</u>	<u>\$ 20,891</u>	<u>\$ 56,485</u>	<u>12</u>	<u>28</u>

<u>12 Months or More</u>	<u>Unrealized loss</u>		<u>Fair value</u>		<u>Number of securities</u>	
	<u>2019</u>	<u>2018</u>	<u>2019</u>	<u>2018</u>	<u>2019</u>	<u>2018</u>
Mortgage-backed securities:						
RMBS.....	\$ -	\$ -	\$ 25	\$ -	1	-
CMBS.....	(274)	-	7,852	-	12	-
Asset-backed securities.....	(2)	-	1,220	-	1	-
US Government and government agency..	(1)	-	1,097	-	2	-
Corporate and other.....	(230)	-	24,072	-	19	-
US states & political subdivisions.....	-	-	-	-	-	-
Total debt securities.....	<u>\$ (507)</u>	<u>\$ -</u>	<u>\$ 34,266</u>	<u>\$ -</u>	<u>35</u>	<u>-</u>
Total other invested assets.....	<u>\$ (140)</u>	<u>\$ -</u>	<u>\$ 3,065</u>	<u>\$ -</u>	<u>1</u>	<u>-</u>

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7. Notes Payable and Interest

As part of the consideration paid in connection with the effective defeasance, or in-substance commutation, of certain of the Company's guarantees of CDS contracts pursuant to the 2009 MTA discussed in Note 3, on July 15, 2009, SGI issued \$150.0 million face amount of short-term and \$475.0 million face amount of long-term surplus notes to the counterparties of such CDS contracts. Subsequent to their issuance, \$142.5 million of paid-in-kind interest has been added to the face amount of the surplus notes. As part of the 2012 settlement of RMBS-related claims and other claims with Bank of America Corp. ("BAC") and affiliates thereof, \$48.4 million face amount of surplus notes (\$21.2 million short-term and \$27.2 million long-term) were received back from the Company which included \$7.7 million of paid-in-kind interest. In addition, in connection with the August 12, 2016 restructuring, the total face amount of the short-term and long-term notes was reduced by \$33.5 million as a result of the discount received and the surplus note payment and \$40.0 million of surplus notes (\$31.5 million and \$8.5 million of long-term and short-term surplus notes, respectively) were reallocated to external parties, which resulted in no change to the par value outstanding. Furthermore, the total notes were reduced by \$296.1 million in connection with subsequent payments made. The total face amount of the surplus notes held by third parties as of March 31, 2019 is \$150.1 million. The short-term surplus notes have a 5.00% interest rate and matured on December 28, 2011, and the long-term surplus notes have a 6.00% interest rate and mature on June 27, 2024. The Company recorded the notes at their estimated fair value of \$141.0 million (\$91.2 million for the short-term notes and \$49.8 million for the long-term notes) at the date of their issuance and accretes the discount from the face amount of the notes over the term of the notes using the interest method. The reallocated surplus notes were recorded at fair value on August 12, 2016 with the discount also accreting over the term of the notes using the interest method. The estimated yield-to-maturity used for both notes was 31.88% at origination; as a result of the August 12, 2016 restructuring, the estimated yield-to-maturity on the long-term surplus notes is 30.11%. The estimated yield-to-maturity on the reallocated surplus notes (long-term surplus notes only) is 12.64%. Interest expense is recognized on the accrual basis using the effective interest rate method. Accretion is recorded as interest expense which is reflected in the accompanying consolidated statements of operations.

On March 28, 2019 the NYDFS approved a net payment of \$169.9 million, which represents the remaining principal and accrued interest on SGI's surplus notes through the payment date, which was April 30, 2019.

See table below for additional information on the surplus notes, accrued interest thereon, and interest expense as of March 31, 2019 and 2018 and December 31, 2018 and for the three months ended March 31, 2019 and 2018:

(U.S. dollars in thousands)	Total		Short-term		Long-term	
	2019	2018	2019	2018	2019	2018
Interest expense:						
Accretion of debt discount	\$ 3,235	\$ 12,425	\$ -	\$ -	\$ 3,235	\$ 12,425
Interest accrual	2,493	12,048	448	2,180	2,045	9,868
Interest expense, including accretion of debt discount	5,728	24,473	448	2,180	5,280	22,293
Notes payable and accrued interest, beginning of period	120,678	556,216	34,650	168,826	86,028	387,390
Notes payable and accrued interest, end of period	<u>\$ 126,406</u>	<u>\$ 580,689</u>	<u>\$ 35,098</u>	<u>\$ 171,006</u>	<u>\$ 91,308</u>	<u>\$ 409,683</u>
Notes payable, end of period	\$ 107,441	\$ 104,206	\$ 22,236	\$ 22,236	\$ 85,205	\$ 81,970
Accrued interest, end of period	18,965	16,472	12,862	12,414	6,103	4,058
Notes payable and accrued interest, end of period	<u>\$ 126,406</u>	<u>\$ 120,678</u>	<u>\$ 35,098</u>	<u>\$ 34,650</u>	<u>\$ 91,308</u>	<u>\$ 86,028</u>
Par value of notes payable, end of period	<u>\$ 150,137</u>	<u>\$ 150,137</u>	<u>\$ 22,236</u>	<u>\$ 22,236</u>	<u>\$ 127,901</u>	<u>\$ 127,901</u>

Interest on the short-term and long-term surplus notes is payable semi-annually, on June 27th and December 28th of each year (commencing December 28, 2009). Such interest was payable in cash or in-kind at the election of the Company through June 27, 2011 (June 27, 2013 for the long-term notes). Interest subsequent to June 27, 2011 (June 27, 2013 for the long-term notes) is required to be paid in cash, subject in each case to the prior approval of the NYDFS. Accordingly, any interest not approved for payment by the NYDFS on or after December 28, 2011 was not capitalized on the outstanding principal balance reflected above, but will accrue interest at the existing rate. The outstanding principal balance of the short-term surplus notes as of June 27, 2011 also will separately accrue interest at such rate.

In addition, SGI was obligated by the terms of its long-term surplus notes to pay interest on the outstanding principal balance of \$475 million together with paid-in-kind interest. Accordingly, any interest not approved for payment by the NYDFS on or after December 28, 2013 was not capitalized on the outstanding principal balance reflected above, but will accrue interest at the existing

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rate. The outstanding principal balance of the long-term surplus notes as of June 27, 2013 also will separately accrue interest at such rate.

In connection with the August 12, 2016 restructuring transactions, \$30.0 million of long-term and short-term surplus notes were transferred from the Company to SGI, and cancelled by SGI. \$23.6 million and \$6.4 million of long-term and short-term notes, respectively (including principal, paid-in-kind interest and accrued interest) of surplus notes were cancelled. In addition, upon closing of the transaction, SGI made a net cash payment of \$55.0 million on its long-term and short-term externally held surplus notes after receiving approval from the NYDFS for such payment.

8. Preferred and Common Shares

Non-Controlling Interest in Subsidiary – Series B Perpetual Non-Cumulative Preferred Shares of SGI

On February 11, 2008, Syncora Guarantee Re Ltd., a former affiliate of SGI issued 2,000 shares of non-cumulative perpetual Series B preferred shares (the “Series B Preferred Shares”) for consideration aggregating \$200 million pursuant to the exercise of a put option under its capital facility. The put option fair value was \$180.0 million at date of exercise. Upon the exercise of the put option, the Company reduced the amount of the Series B Preferred Shares by such amount. Accordingly, the original carrying value of the Series B Preferred Shares of \$20.0 million represented the net proceeds received upon the issuance less the reversal of the fair value of the put option on the date of exercise. After the merger of Syncora Guarantee Re Ltd. with and into SGI, the Series B Preferred Shares became preferred shares of SGI. The Series B Preferred Shares have a par value of \$120 per share and a liquidation preference of \$100,000 per share. Holders of outstanding Series B Preferred Shares are entitled to receive, in preference to the holders of SGI’s common shares non-cumulative cash dividends, when, as and if declared by the board of directors, at a percentage rate per Series B Preferred Share for any dividend period ending on or prior to December 9, 2009, one-month LIBOR plus 1.00% per annum, calculated on an actual/360 day basis; and for any subsequent dividend period, one-month LIBOR plus 2.00% per annum, calculated on an actual/360 day basis.

Upon any voluntary or involuntary liquidation, dissolution or winding-up of SGI, each holder of Series B Preferred Shares is entitled to payment of any amount equal to the liquidation preference per share, plus accrued and unpaid dividends thereon (to the extent declared), if any, to the date of distribution in preference to holders of SGI’s common shares. Neither the merger or consolidation of SGI (as successor to Syncora Guarantee Re Ltd.) into or with any other company, the merger of any other company into SGI, nor the sale, lease or conveyance of all or substantially all of the property or business of SGI shall alone be deemed to be a dissolution, liquidation or winding up of SGI.

The holders of the Series B Preferred Shares are not entitled to any voting rights as shareholders of SGI and their consent is not required for taking any corporate action. Subject to certain requirements, the Series B Preferred Shares may be redeemed, in whole or in part, at the option of SGI at any time or from time to time after December 9, 2009 for cash at a redemption price equal to the liquidation preference per share plus any accrued and unpaid dividends thereon to the date of redemption without interest on such unpaid dividends. SGI has not declared or paid dividends on the Series B Preferred Shares during the year ended December 31, 2018 and 2017. As a result of the BAC settlement, SGI holds 655 shares of its non-cumulative perpetual Series B preferred shares, which were transferred by BAC to SGI.

On January 14, 2019, SGI made a one-time purchase from third parties of \$76.4 million of aggregate face amount of Pass-Through Trust Preferred Securities issued by the Twin Reefs Pass-Through Trust for \$64.9 million, leaving outstanding \$58.1 million of aggregate face amount of Twin Reefs Securities held by third parties. The Twin Reefs Securities purchased correspond to 764 shares of SGI’s Series B preferred shares. As a result of this purchase and based on accounting guidance for extinguishment of preferred shares, the Company recorded an increase to accumulated deficit for the difference between the cash paid and reduction to the carrying value of the Series B preferred shares for the three months ended March 31, 2019. For purposes of earnings per share to common shareholders in the three months ended March 31, 2019, this purchase was reflected as a reduction to net income available to common shareholders.

As of March 31, 2019, as a result of the above purchase, SGI currently holds 1,419 shares of its issued 2,000 Series B preferred shares, which includes the previously held 655 shares transferred to SGI from BAC in connection with the BAC settlement.

Common Shares

In connection with the Company’s previously reported 2012 settlement of RMBS-related claims and other claims with BAC and affiliates thereof, the Company reported that as part of such settlement, subsidiaries of BAC transferred or agreed to transfer to SGI or its designee certain of SGI’s and the Company’s preferred shares, surplus notes and other securities. The transfer of the Company’s common shares and preferred shares had remained subject to the Company’s board approval and with respect to the preferred shares, regulatory approval. During the fourth quarter of 2014, 3,044,588 of Syncora Holdings’ common shares were

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transferred from BAC to SGI and such shares are accounted for and held as treasury shares by the Company, but remain legally outstanding for voting and other purposes. See Note 13 for further discussion on dividend restrictions.

On August 12, 2016, in connection with the restructuring transaction, in the aggregate, the Company issued 30.3 million of additional common shares, which were recorded at a fair value of \$37.9 million.

9. Accumulated Other Comprehensive Income

Changes in accumulated other comprehensive income for the three months ended March 31, 2019 and 2018 by component are as follows:

(U.S. dollars in thousands)	Total		Available-for-sale securities		Unrecognized pension and post-retirement costs	
	2019	2018	2019	2018	2019	2018
	Other comprehensive (loss) income before reclassifications	\$ 9,744	\$ (219)	\$ 9,744	\$ (239)	\$ -
Amounts reclassified from accumulated other comprehensive income:						
Realized losses (gains) on sale of securities.....	26	(10,296)	26	(10,296)	-	-
Cumulative effect of change in accounting principle for equity securities.....	-	(7,469)	-	(7,469)	-	-
Other-than-temporary impairments.....	237	(2,556)	237	(2,556)	-	-
Current period other comprehensive (loss) income, net.....	10,007	(20,540)	10,007	(20,560)	-	20
Balance, Beginning.....	1,828	31,015	1,828	30,663	-	352
Balance, Ending.....	<u>\$ 11,835</u>	<u>\$ 10,475</u>	<u>\$ 11,835</u>	<u>\$ 10,103</u>	<u>\$ -</u>	<u>\$ 372</u>

10. Income Taxes

Syncora Holdings is not subject to any taxes in Bermuda on either income or capital gains under current Bermuda law. In the event that there is a change such that these taxes are imposed, Syncora Holdings would be exempted from any such tax until March 2035 pursuant to Bermuda law.

As the Company is a Bermuda corporation and, except for gross basis withholding taxes on U.S. source investment income, neither it nor its non-U.S. subsidiaries have paid U.S. Federal corporate income taxes, on the basis that they are not engaged in a trade or business or otherwise subject to taxation in the United States. However, because definitive identification of activities which constitute being engaged in a trade or business in the United States is not provided by the Internal Revenue Code of 1986, as amended, regulations or court decisions, there can be no assurance that the Internal Revenue Service would not contend that the Company or its non-U.S. subsidiaries are engaged in a trade or business or otherwise subject to taxation in the United States.

In addition to the foregoing, there is a risk that the Internal Revenue Service could disagree with a number of tax positions taken by the Company with respect to certain transactions, including but not limited to, certain transactions undertaken in connection with the 2009 MTA. If any of the positions taken by the Company were successfully challenged by the Internal Revenue Service, there could be a material adverse effect on the amount of U.S. NOLs available to the Company to offset future taxable income.

SGI files a consolidated U.S. federal tax return with Syncora Holdings U.S. Inc. (the U.S. common parent of the Syncora Holdings' group) and its subsidiaries (which consists of SGI and Syncora Holdings U.S. Inc.'s other U.S. based subsidiaries). Syncora Holdings U.S. Inc. maintains a tax sharing agreement with its subsidiaries, whereby each subsidiary determines its payment due to/from Syncora Holdings U.S., Inc. on a separate company return basis. Further, if the subsidiary's separate return computation results in a taxable loss for the period, Syncora Holdings U.S., Inc. is obligated to reimburse the subsidiary to the extent that such loss reduces the Company's consolidated income tax liability. The tax sharing agreement calls for the reimbursement to take place within thirty days of Syncora Holdings filing its federal consolidated tax return.

The Company's income tax provision for the three months ended March 31, 2019 and 2018 was approximately \$0.5 million and zero, respectively. In accordance with U.S. GAAP, for the three months ended March 31, 2019 and 2018, the Company recorded income tax based on the estimated effective tax rate for the full year 2019 and 2018.

As of March 31, 2019 and December 31, 2018, respectively, the Company had no unrecognized tax benefits and no adjustments to liabilities or operations were required.

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The Company recognizes interest and penalties related to uncertain tax positions in income tax expense, which were zero for the three months ended March 31, 2019 and 2018. Tax years 2015 through 2018 are subject to examination by U.S. federal authorities. There are currently no state or local tax audits underway for the Company as of March 31, 2019.

At March 31, 2019, the Company had net operating loss carryforwards expiring from 2027 through 2038 of \$2.7 billion.

At March 31, 2019, the Company had capital loss carryforwards of \$142.5 million expiring from 2019 through 2023.

The most significant items giving rise to deferred tax assets as of March 31, 2019 are Syncora Holdings' and Syncora Guarantee's net operating loss and capital loss carryforwards which are offset by a full valuation allowance.

Management has concluded that results from operations forecasted to be generated in the future are more likely than not insufficient to permit realization of the Company's U.S. deferred tax assets, thus a valuation allowance has been established against the entire U.S. deferred tax assets of the Company at March 31, 2019 and December 31, 2018. The valuation allowance was calculated in accordance with the provisions of the accounting pronouncements for income taxes, which place primary importance on operating results in recent periods when assessing the need for a valuation allowance. The Company intends to maintain a full valuation allowance for its net U.S. deferred tax assets until sufficient positive evidence exists to support reversal of all or a portion of the valuation allowance.

As of March 31, 2019 and December 31, 2018, the Company recorded net deferred tax liabilities of \$0.1 million and \$0.1 million, respectively, and are included in "Other liabilities" on the Company's consolidated balance sheets.

At March 31, 2019, the Company's cumulative NOLs, which may be carried forward to offset future taxable income, are \$2.7 billion. The Company's ability to utilize its NOLs at March 31, 2019 expires from 2027 through 2038. Approximately \$161.3 million of the Company's NOLs are subject to limitation under Section 382 of the Internal Revenue Code ("Section 382") as a result of an ownership change, as defined under that code section that occurred on August 5, 2008. An ownership change, as defined under Section 382 generally occurs if the percentage stock ownership of shareholders owning (or deemed under Section 382 to own) 5% or more of Syncora Holdings' common shares increases by more than 50 percentage points over the lowest percentage of Syncora Holdings' common shares owned by such shareholders during a defined period of time. To avoid an ownership change in the future and further limitation on the use of the Company's NOLs, on October 21, 2008, Syncora Holdings' Board of Directors approved changes to Syncora Holdings' Bye-laws which were subsequently approved by the shareholders on February 9, 2009 to limit the transfer of shares prior to the expiration of certain time periods specified in such Bye-laws.

In connection with the Restructuring Transactions completed on August 12, 2016, pursuant to an amended and restated tax sharing agreement, SGI reallocated \$1.75 billion of excess net operating losses to Syncora Holdings US Inc. for its sole use and benefit, where these net operating losses may be used more broadly. In addition, Syncora Holdings US Inc. provided contractual protections relating to the preservation and utilization of SGI's retained net operating losses. The amendments to the tax sharing agreement did not have any effect on the Company's consolidated financial results.

The Company's significant NOLs may reduce future U.S. tax liabilities that otherwise would be payable by the Company. The ability to utilize these NOLs would be limited in certain events, including if an "ownership change" under Section 382 were to occur. Section 382 limits the ability of a corporation that experiences an ownership change to utilize its NOLs and certain built-in losses after the ownership change. An ownership change is generally any change in ownership of more than 50 percentage points of a corporation's stock over a rolling 3-year period. These rules generally operate by focusing on ownership changes among shareholders owning directly or indirectly 5% or more of the stock of a corporation (including for this purpose certain groupings of shareholders each of whom owns less than the 5% threshold) or any change in ownership arising from a new issuance or a redemption of stock by the corporation. Generally under Section 382, in the event of an ownership change, the amount of taxable income that a corporation can offset by its "pre-change losses" (which include its NOLs) is restricted to an annual amount equal to the equity value of the corporation immediately prior to the ownership change multiplied by the long-term tax-exempt rate. These limitations generally prohibit transactions that result in the creation of a new 5% shareholder or increases the ownership interest of an existing 5% shareholder. A 5% shareholder for this purpose is defined in Syncora Holdings bye-laws by reference to Section 382 and the Treasury Regulations issued thereunder, and includes "public groups". A prohibited transaction under Syncora Holdings bye-laws is void at inception.

11. Financial Instruments and Fair Value Measurements and Disclosures

A number of the Company's financial instruments are carried at fair value with changes in fair value recognized in earnings or loss each period. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (an exit price). In determining fair value, the Company uses various valuation techniques and considers the fair value hierarchy.

The fair value hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical instruments (Level 1) and the lowest priority to valuation techniques using unobservable inputs (Level 3). Observable inputs are inputs that market participants would use in pricing the financial instruments that are based on market data obtained from sources independent of the Company. Unobservable inputs reflect the Company's estimates of the assumptions market participants would use in pricing the financial instruments based on the best information available in the circumstances. These valuation techniques involve some level of management estimation and judgment. The degree to which management's estimation and judgment is required is generally dependent upon the market price transparency for the instruments, the availability of observable inputs, frequency of trading in the instruments and the instrument's complexity.

In measuring the fair market values of its financial instruments, the Company maximizes the use of observable inputs and minimizes the use of unobservable inputs based on the fair value hierarchy. The hierarchy is categorized into three levels based on the reliability of inputs as follows:

Level 1—Unadjusted quoted prices for identical instruments in active markets. The Company generally defines an active market as a market in which trading occurs at significant volumes. Active markets generally are more liquid and have a lower bid-ask spread than an inactive market.

Level 2—Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and observable inputs other than quoted prices, such as interest rates or yield curves and other inputs derived from or corroborated by observable market inputs.

Level 3—Model derived valuations in which one or more significant inputs or significant value drivers are unobservable. Financial instruments are considered Level 3 when their values are determined using pricing models, discounted cash flow methodologies or similar techniques and at least one significant model assumption or input is unobservable. Level 3 financial instruments also include those for which the determination of fair value requires significant management judgment or estimation.

A description of the valuation techniques applied to the Company's assets and liabilities measured at fair value follows:

Valuation Techniques — Credit Default Swap Contracts

The principal drivers of the fair value of the Company's CDS contracts include: (i) general market credit spreads for the type(s) of assets referenced in CDS contracts, (ii) the specific quality and performance of the actual assets referenced in the contracts, (iii) the amount of subordination in the transaction before the Company's liability attaches, (iv) other customized structural features of such contracts (*e.g.*, terms, conditions, covenants), (v) supply and demand factors, including the volume of new issuance, and (vi) the market perception of the Company's ability to meet its obligations under its CDS contracts which is factored into the Company's fair value estimates as discussed below.

The fair value of the Company's in-force portfolio of CDS contracts represents the net present value of the difference between the remaining uncollected premiums that the Company originally charged for credit protection and management's best estimate of what a financial guarantor of comparable credit worthiness would hypothetically charge to provide the same protection as of the measurement date. The hypothetical nature of this exit value is representative of the lack of a principal market for the Company's CDS contracts. In the absence of such a principal market, the Company believes other financial guarantors of comparable credit quality to the Company best represent the hypothetical exit market for the Company's CDS contracts. Fair value is defined as the price at which an asset or a liability could be bought or transferred in a current transaction between willing parties. Fair value is determined based on quoted market prices, if available. Quoted market prices are available only on a limited portion of the Company's in-force portfolio of CDS contracts. If quoted market prices are not available, fair value is estimated based on valuation techniques involving management's judgment. In determining the fair value of its CDS contracts, the Company uses various valuation approaches with priority given to observable market prices when they are available. Market prices are generally available for traded securities and market standard CDS contracts but are less available or unavailable for highly-customized CDS contracts. Most of the Company's

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CDS contracts are highly customized structured credit derivative transactions that are not traded and do not have observable market prices.

Key variables used in the Company's valuation of substantially all of its CDS contracts include the balance of unpaid notional, expected remaining term, fair values of the underlying reference obligations, reference obligation credit ratings, assumptions about current financial guarantee CDS fee levels relative to reference obligation spreads, the Non-Performance Risk (as defined and described below) of its in-force CDS contract exposure, and other factors. Fair values of the underlying reference obligations are obtained from broker quotes when available, or are derived from other market indications such as new issuance and secondary spreads and quoted values for similar transactions and indices. The Company's valuation of such CDS contracts does not generally provide for any adjustment to broker quotes. While such broker quotes are non-binding, the brokers from whom the Company obtains such quotes actively monitor and participate in the markets where such collateral is traded. Accordingly, the Company believes that such brokers rely on observable market information to the greatest extent possible when determining such quotes; however, such brokers may also rely on their internal models and unobservable inputs in making such determinations.

Implicit in the fair values obtained by the Company on the underlying reference obligations are the market's assumptions about default probabilities, default timing, correlation, recovery rates and collateral values. In general, the Company is using a percentage of the credit spread over proxy index (the "premium percentage") that management believes is consistent with (i) historical premium pricing for high credit spread transactions and (ii) levels attainable in the market just prior to the collapse of the market for CDS from financial guarantors. This data indicates that this premium percentage decreases as a function of increasing underlying credit spreads. A component of this relationship is the lack of liquidity reflected in the credit spread (the liquidity premium) that has historically flowed directly to the CDS counterparty as the funding institution and to cover the funders' additional funding costs and risks. Using the historical data available, a regression analysis was completed to determine the approximate rate of change of the premium percentage as underlying credit spreads move up and down. The resulting relationship from these analyses were applied to the current credit spread levels of the underlying reference securities, or their proxy index, to generate the expected current premium for each outstanding CDS.

In addition to that discussed above, the fair value of the Company's CDS contracts reflects the risk that SGI, as applicable, will not be able to honor its obligations under its CDS contracts, or its Non-Performance Risk. Generally, the Company would measure Non-Performance Risk as implied by the market price of buying credit protection on SGI as applicable. Since SGI does not have an observable market credit spread, SGI estimates its Non-Performance Risk based on the market observable credit spreads of comparable financial guarantee insurance companies. However, management reviews these spreads every quarter and makes adjustments as necessary. These adjustments may include eliminating idiosyncratic events specific to a particular company included in the market index, and focusing solely on spreads that represent a more suitable proxy for SGI's own credit risk. Management uses its judgment in making those adjustments, which are inherently subjective and judgmental in nature.

Such Non-Performance Risk was reflected in the fair value of SGI's CDS contracts by incorporating the estimated spreads at which the CDS contracts would trade on SGI, as discussed above, into the discount rate used. SGI estimated a discount rate for each CDS contract based on the swap rate and its estimated credit spread for the duration that is the closest to the remaining weighted average life of the obligation referenced in the CDS contract.

Since the estimate of fair value of the Company's CDS contracts reflects significant unobservable inputs related to the estimate of the Company's Non-Performance Risk and lack of market observable data, the Company's CDS contracts are categorized in Level 3 of the fair value hierarchy.

Valuation Techniques — Interest Rate Swap Guarantees

The Company's interest rate swap exposure consists primarily of financial guarantees that cover one party's payment obligations to another party under an interest rate swap contract. These interest rate swap guarantees are considered derivative financial instruments and are recorded at fair value. The fair value of these interest rate swap guarantees is included in the caption "credit default and other swap contracts, at fair value" on the consolidated balance sheets.

The Company's interest rate swap guarantees cannot be legally traded and do not have observable market prices. The Company determines fair value based on valuation techniques involving management's judgment using internal valuation models. The estimated fair value of the interest rate swap guarantees are primarily based upon unobservable inputs, including estimated default probabilities of the obligor, contractual terms, estimated recovery rates and the application of credit value adjustments for the Company's own non-performance risk.

Since the estimate of fair value of the Company's interest rate swap guarantees reflects significant unobservable inputs, the Company's interest rate swap contracts are categorized in Level 3 of the fair value hierarchy.

Valuation Techniques — VIE Assets and Liabilities

The consolidated VIE assets and liabilities consist primarily of RMBS securities. The fair value of the Company's consolidated VIE assets and liabilities is determined based on quoted market prices, if available. When observable quoted market prices are not available, fair value is determined based on internal discounted cash flow valuation models. The inputs to the valuation models primarily include estimated prepayment rates, market values of the underlying collateral, estimated default rates, market yields, credit spread indices, discount rates, estimated recovery rates, and for those liabilities insured by the Company, the benefit from the Company's insurance policy guaranteeing timely principal and interest for the VIE assets insured by the Company and the application of credit value adjustments for the Company's own non-performance credit risk. Since the majority of the significant inputs are unobservable, which reflect the Company's estimates of market assumptions, the fair value measurements of the consolidated VIE assets and liabilities are categorized as Level 3 in the fair value hierarchy.

Valuation Techniques — Debt Securities Available for Sale

U.S. Government and government agencies

U.S. Treasury securities are valued using unadjusted quoted market prices. Accordingly, U.S. Treasury securities are generally categorized in Level 1 of the fair value hierarchy. U.S. government agency securities are generally valued using quoted market prices obtained from an independent third-party investment service provider. U.S. government agency securities are generally categorized in Level 2 of the fair value hierarchy.

Mortgage and asset-backed securities

Mortgage and asset-backed securities are generally valued based on quoted prices or spread data, which are obtained from an independent third-party investment service provider. Mortgage and asset-backed securities are generally categorized in Level 2 of the fair value hierarchy. If external prices or significant inputs are unobservable, the Company will determine fair value using its own internal model estimates. In such cases, mortgage and asset-backed securities are categorized in Level 3 of the fair value hierarchy.

Corporate

The fair value of corporate bonds is determined using recently executed transactions or market price quotations obtained from an independent third-party investment service provider. Corporate bonds are generally categorized in Level 2 of the fair value hierarchy. If external prices or significant inputs are unobservable, the Company will determine fair value using its own internal model estimates. In such cases, these corporate securities are categorized in Level 3 of the fair value hierarchy.

U.S. State and political subdivisions

The fair value of state and municipal securities is determined using recently executed transactions or market price quotations obtained from an independent third-party service provider. These bonds are generally categorized in Level 2 of the fair value hierarchy. If external prices or significant inputs are unobservable, the Company will determine fair value using its own internal model estimates. In such cases, these state and municipal securities are categorized in Level 3 of the fair value hierarchy.

Valuation Techniques — Cash and Cash Equivalents and Restricted Cash and Cash Equivalents

The carrying amounts of these items approximate fair value due to the short-term maturity of these instruments. Cash and cash equivalents include deposits in banks, commercial paper, money market accounts and money market funds, for which fair value of these instruments is based upon quoted market prices. The Company does not adjust the quoted market price for such instruments. Cash and cash equivalents are categorized in Level 1 of the fair value hierarchy.

Valuation Techniques — Other Invested Assets

Other invested assets primarily include direct investments in equity securities and exchange-traded direct equity investments. Equity securities and exchange-traded equity securities are generally valued based on quoted prices. Such investments are categorized in Level 1 of the fair value hierarchy. Investments in certain funds that are not actively traded but have inputs that are observable in the market or can be derived principally from observable market data are categorized in Level 2 of the fair value hierarchy. If external prices or significant inputs are unobservable, the Company will determine fair value using its own internal model estimates. In such cases, these other invested assets are categorized in Level 3 of the fair value hierarchy.

Valuation Techniques — Other Receivable – City of Detroit

The carrying amount of the City of Detroit credit certificate is carried at fair value, which is included on the accompanying consolidated balance sheets in “other assets”. The Company determines the fair value of this certificate using its own internal model incorporating estimated selling prices and any available market information. The most significant unobservable input is the credit and illiquidity discount which primarily ranges from 0% to 50%. Due to the limited availability of market information, the fair value could be subject to significant volatility. The inputs used in determining the fair value were mostly unobservable and as a result, the fair value of this certificate is categorized into the Level 3 hierarchy.

Valuation Techniques — Financial Guarantee Insurance Contracts

The Company believes that the best estimate of fair value for its entire portfolio of insurance contracts is the discounted expected premiums less the discounted expected losses over the remaining life of each contract. To determine this fair value, the Company utilized a discounted cash flow model based on inputs that include assumptions of expected losses net of expected recoveries where loss reserves have been established (reserve contracts), and expected premiums and losses where loss reserves have not been recognized (non-reserve contracts). For non-reserve contracts, estimates of expected loss are driven by assumptions as to default and loss given default rates for each contract. Market-based discount rates that are credit adjusted for the premium payer and the Company's own credit risk are applied to the premium and loss cash flows, respectively, to ultimately determine the contract's fair value. The inputs used in determining fair value were mostly unobservable and as a result the fair value could change materially.

The fair value of the Company's financial guarantee insurance contracts related to its retained business was \$73.7 million and \$49.9 million at March 31, 2019 and December 31, 2018, respectively. The fair value of the Company's insurance contracts would be categorized into the Level 3 hierarchy since the significant inputs used were unobservable.

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Fair Value Hierarchy Tables

The following fair value hierarchy table presents information about the Company's assets and liabilities measured at fair value on a recurring basis as of March 31, 2019 and December 31, 2018:

(U.S. dollars in thousands)	Quoted Prices in Active Markets for Identical Assets (Level 1)		Significant Other Observable Inputs (Level 2)		Significant Unobservable Inputs (Level 3)		Total Assets / Liabilities at Fair Value	
	2019	2018	2019	2018	2019	2018	2019	2018
ASSETS								
Debt securities available for sale:								
Mortgage and asset-backed securities								
RMBS.....	\$ -	\$ -	\$ 77,455	\$ 70,523	\$ 1,410	\$ 1,515	\$ 78,865	\$ 72,038
CMBS.....	-	-	37,689	29,173	-	-	37,689	29,173
Asset-backed securities.....	-	-	75,789	65,104	-	-	75,789	65,104
U.S. Government and government agencies.....	63,672	95,614	-	-	-	-	63,672	95,614
Corporate and other.....	-	-	338,007	316,268	-	-	338,007	316,268
U.S. states and political subdivisions.....	-	-	33,733	35,291	-	-	33,733	35,291
Total debt securities available for sale.....	63,672	95,614	562,673	516,359	1,410	1,515	627,755	613,488
Other invested assets.....	81,609	74,336	5,000	5,017	8,032	8,151	94,641	87,504
Cash and cash equivalents.....	60,179	150,388	5,378	-	-	-	65,557	150,388
Restricted cash and cash equivalents.....	13,699	10,632	-	-	-	-	13,699	10,632
Assets of consolidated variable interest entities.....	-	-	-	-	19,407	20,843	19,407	20,843
Credit default and other swap contracts.....	-	-	-	-	226,204	227,052	226,204	227,052
Total assets.....	\$ 219,159	\$ 330,970	\$ 573,051	\$ 521,376	\$ 255,053	\$ 257,561	\$ 1,047,263	\$ 1,109,907
LIABILITIES								
Credit default and other swap contracts.....	\$ -	\$ -	\$ -	\$ -	\$ 237,053	\$ 235,541	\$ 237,053	\$ 235,541
Liabilities of consolidated variable interest entities.....	-	-	-	-	316	340	316	340
Total liabilities.....	\$ -	\$ -	\$ -	\$ -	\$ 237,369	\$ 235,881	\$ 237,369	\$ 235,881

Level 3 Assets and Liabilities Reconciliation Tables

Level 3 Assets

The following table provides a reconciliation of the Company's assets measured at fair value on a recurring basis using unobservable inputs (Level 3) as of March 31, 2019 and 2018:

(U.S. dollars in thousands)	Debt Securities Available for Sale					
	Mortgage and Asset- Backed Securities		Corporate and Other		Other Invested Assets	
LEVEL 3 ASSETS	2019	2018	2019	2018	2019	2018
Balance, beginning of period.....	\$ 1,515	\$ 2,217	\$ -	\$ 45,444	\$ 8,151	\$ 40,504
Realized gains (losses).....	44	2,172	-	4,872	(119)	(8)
Unrealized gains (losses) included in earnings.....	-	-	-	6,113	-	-
Unrealized gains (losses) included in OCI.....	(159)	1,096	-	(9,501)	-	(56)
Purchases.....	136	2,029	-	54	-	-
Sales.....	(126)	(4,479)	-	(46,982)	-	-
Transfers into (out of) Level 3.....	-	-	-	-	-	-
Balance, end of period.....	\$ 1,410	\$ 3,035	\$ -	\$ -	\$ 8,032	\$ 40,440

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	Other Assets		Assets of Consolidated Variable Interest Entities		Credit default and other swap contracts	
	2019	2018	2019	2018	2019	2018
	LEVEL 3 ASSETS					
Balance, beginning of period.....	\$ -	\$ 3,007	\$ 20,843	\$ 118,154	\$ 227,052	\$ -
Deconsolidation of VIEs.....	-	-	-	(35,207)	-	-
Realized gains (losses).....	-	(241)	-	-	-	-
Unrealized gains (losses) included in earnings.....	-	-	(1,436)	(8,382)	(848)	-
Unrealized gains (losses) included in OCI.....	-	-	-	-	-	-
Purchases.....	-	-	-	-	-	-
Sales.....	-	-	-	-	-	-
Distributions.....	-	-	-	(34,634)	-	-
Transfers into (out of) Level 3.....	-	-	-	-	-	-
Balance, end of period.....	\$ -	\$ 2,766	\$ 19,407	\$ 39,931	\$ 226,204	\$ -

There were no transfers into or out of Level 3 during the three months ended March 31, 2019 and 2018.

Level 3 Liabilities

The following table provides a reconciliation for the Company's liabilities measured at fair value on a recurring basis using unobservable inputs (Level 3) for the three months ended March 31, 2019 and 2018:

(U.S. dollars in thousands)	Credit Default and Other Swap Contracts		Contingent Consideration		Liabilities of Consolidated Variable Interest Entities	
	2019	2018	2019	2018	2019	2018
LEVEL 3 LIABILITIES						
Balance, beginning of period.....	\$ 235,541	\$ 104,094	\$ -	\$ 2,043	\$ 340	\$ 60,708
Deconsolidation of VIEs.....	-	-	-	-	-	(35,207)
Payment of contingent consideration.....	-	-	-	(2,043)	-	-
Realized (gains) losses.....	(69)	(799)	-	-	-	-
Unrealized (gains) losses included in earnings.....	1,581	22,919	-	-	(24)	(3,981)
Balance, end of period.....	\$ 237,053	\$ 126,214	\$ -	\$ -	\$ 316	\$ 21,520

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The following table provides quantitative information regarding the significant unobservable inputs used to measure the fair value of the Company's Level 3 assets and liabilities on a recurring basis as of March 31, 2019 and December 31, 2018:

(U.S. dollars in thousands)

Level 3 Assets / Liabilities	Fair Value		Valuation Techniques	Significant Unobservable Inputs	Range of Inputs	
	2019	2018			2019	2018
Assets						
Mortgage- and asset-backed securities	\$ 1,410	\$ 1,515	Discounted cash flows	Constant prepayment rate Constant default rate Loss severity Yield	3.9% - 16% 3.0% - 35% 40% - 100% 4.75% - 7.25%	1.16% - 16% 1.44% - 35% 40% - 100% 5.0% - 7.5%
Other invested assets	8,032	8,151	Market approach	Liquidation preference	\$4.9 million	\$4.9 million
Assets of consolidated VIEs	19,407	20,843	Discounted cash flows	Constant prepayment rate Constant default rate Loss severity Yield Non-performance risk	2.65% - 99.86% 2.08% - 35.00% 40% - 100% 4.75% - 7.25% 5.09% - 5.40%	1.16% - 36.04% 1.44% - 35.00% 40% - 100% 5.0% - 7.50% 5.36% - 6.86%
Credit default and other swap contracts	226,204	227,052	Discounted cash flows	Loss severity Default rate Market premiums Weighted average life Non-performance risk	10% - 60% 0.06% - 1.11% 30 bps - 241 bps 1.32 yrs - 34.30 yrs 2.70% - 3.82%	10% - 60% 0.02% - 1.11% 35 bps - 235 bps 0.5 yrs - 34.6 yrs 2.99% - 4.50%
Liabilities						
Credit default and other swap contracts	\$237,053	\$235,541	Discounted cash flows	Loss severity Default rate Market premiums Weighted average life Non-performance risk	10% - 60% 0.06% - 1.11% 30 bps - 241 bps 1.32 yrs - 34.30 yrs 2.70% - 6.61%	10% - 60% 0.02% - 1.11% 35 bps - 235 bps 0.5 yrs - 34.6 yrs 2.99% - 8.25%
Liabilities of consolidated VIEs	316	340	Discounted cash flows	Constant prepayment rate Constant default rate Loss severity Yield Non-performance risk	4.02% - 99.86% 4.00% - 35.00% 70% - 100% 4.75% - 5.40% 5.09% - 5.40%	2.45% - 36.04% 2.64% - 35.00% 70% - 100% 5.0% - 6.86% 5.36% - 6.86%

The significant unobservable inputs used in the fair value measurement of the Company's assets and liabilities are shown in the table above. Significant changes in any of those inputs noted above in isolation can result in a materially lower or higher fair value measurement.

Non-Performance Risk

The Company considers the effect of nonperformance risk in determining the fair value of its CDS liabilities and the consolidated VIE liabilities. The fair value of the Company's CDS reflects the risk that SGI, as applicable, will not be able to honor its obligations under its CDS contracts, or its Non-Performance Risk. Since SGI does not have an observable market credit spread, SGI measures its Non-Performance Risk based on the market observable credit spread of a comparable financial guarantee insurance company.

The fair value of the Company's consolidated VIE liabilities reflects the Non-Performance Risk that the Company will not be able to honor VIE obligations where VIE liabilities exceed the value of the related pledged assets.

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Set forth below is information regarding the Company's in-force CDS and other swap contracts and VIE liabilities as of March 31, 2019 and December 31, 2018, including the fair value of such contracts and VIE liabilities, the Non-Performance Risk discount on such contracts and VIE liabilities which is embedded in the credit default and other swap contracts and the VIE liabilities on the accompanying consolidated balance sheets:

(U.S. dollars in millions)	<u>CDS and other</u> <u>swap contracts</u>		<u>VIE liabilities</u>	
	<u>2019</u>	<u>2018</u>	<u>2019</u>	<u>2018</u>
Fair value, before giving effect to Non-Performance Risk.....	\$ 293.4	\$ 308.4	\$ 0.3	\$ 0.3
Less:				
Non-Performance Risk.....	<u>56.3</u>	<u>72.9</u>	<u>-</u>	<u>-</u>
Fair value, after giving effect to Non-Performance Risk.....	<u>\$ 237.1</u>	<u>\$ 235.5</u>	<u>\$ 0.3</u>	<u>\$ 0.3</u>

Financial Instruments Not Carried at Fair Value

At March 31, 2019 and December 31, 2018, the carrying value of the Company's surplus notes as described in Note 7 was \$107.4 million and \$104.2 million, respectively. The interest rate on these surplus notes is 5.0% and 6.0% for each series with the first maturity date on such surplus notes scheduled for December 2011 and in June 2024. On March 28, 2019, the NYDFS approved a net payment of \$169.9 million, which represents the remaining principal and accrued interest on SGI's surplus notes and payment was made on April 30, 2019. The fair value of the Company's surplus notes was difficult and complex to estimate as such surplus notes were not listed on any exchange or publicly traded in any market. Any trading activity was inherently limited, and the prices may vary significantly between trades. Based on limited available market data obtained by management, the Company's short-term notes and long-term notes were found to have a price of approximately 97.7 and 98.2, respectively, as of December 31, 2018. These prices were based on total par, paid-in-kind interest and accrued but unpaid interest.

12. Commitments and Contingencies

a. Legal Matters

In the ordinary course of business, the Company may be subject to litigation or other legal proceedings. The Company intends to vigorously defend against any actions in which it is a defendant and against other potential actions, and the Company does not expect the outcome of any such matters to have a material adverse effect on the Company's financial position, results of operations or liquidity. The Company can provide no assurance that the ultimate outcome of these actions will not cause a loss nor have a material adverse effect on the Company's financial position, results of operations or liquidity.

Set forth below is a description of legal proceedings to which Syncora Guarantee is a party.

Puerto Rico

On July 18, 2017, certain creditors of PREPA, including Syncora Guarantee, filed a motion in PREPA's Title III case seeking relief from the automatic stay in order to commence an action to enforce their statutory right to appoint a receiver. On September 14, 2017, this motion was denied by Judge Swain. On September 28, 2017, the Company and the other creditors appealed the decision to the United States Court of Appeals for the First Circuit. On August 8, 2018, the First Circuit issued an opinion vacating Judge Swain's decision and holding that sections 305 and 306 of PROMESA do not preclude the court from granting the requested relief to appoint a receiver. The First Circuit remanded the case back to Judge Swain and allowed the creditors to file a renewed motion to seek relief from the automatic stay.

On October 3, 2018, certain monoline insurers, including Syncora Guarantee, filed a renewed motion in PREPA's Title III case for relief from the automatic stay in order to commence an action to enforce their statutory right to appoint a receiver. On March 27, 2019, the Official Committee of Unsecured Creditors filed an objection to the renewed motion disputing, among other things, the collateral securing the PREPA bonds. On May 10, 2019, the Oversight Board and AAFAF filed a motion to dismiss the renewed motion arguing, among other things, that once the PREPA RSA is approved Assured has agreed to withdraw from the motion. As a result, the remaining movants allegedly lack the required holdings to pursue the motion in accordance with the PREPA trust agreement.

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On August 7, 2017, certain creditors of PREPA, including Syncora Guarantee, filed a complaint in PREPA's Title III case in order to enforce their rights as holders of special revenue bonds. On October 13, 2017, in light of the impact of Hurricane Maria on Puerto Rico, the creditors filed a notice of voluntary dismissal without prejudice.

On May 2, 2019, the Oversight Board and the official committee of unsecured creditors filed a complaint challenging numerous proofs of claims relating to general obligation bonds, including those filed by the Company. Among other things, the complaint disputes the existence, extent, and enforceability of the consensual and statutory liens asserted in the proofs of claim and is seeking to reclassify such claims as unsecured obligations of the Commonwealth.

b. Lease and Other Commitments

The Company entered into a two year lease commitment for office premises at 555 Madison Avenue, New York, New York commencing on December 15, 2018. The Company had lease commitments for office premises at 76 South Orange Avenue, South Orange, New Jersey, which terminated on February 28, 2018 and at 135 West 50th Street, New York, New York, which terminated on January 31, 2019.

Effective April 1, 2018, the Company entered into an amended two year agreement with International Business Machines Corporation for information technology outsourcing services. Fees associated with the agreement are expected to be approximately \$1.0 million in 2019.

Net minimum aggregate lease commitments are \$0.6 million, \$0.5 million, \$22.0 thousand, \$0 and \$0 for the years ended December 31, 2019 through December 31, 2023.

Net rent expense was \$0.2 million and \$0.3 million for the three months ended March 31, 2019 and 2018, respectively.

13. Dividend Restrictions and Insurance Regulatory Requirements

Syncora Holdings

Syncora Holdings' Board of Directors did not declare a quarterly dividend with respect to its common shares for the year ended December 31, 2018 or at any time thereafter through to the issuance date of these financial statements. Any future dividends will be subject to the discretion and approval of the Syncora Holdings' Board of Directors, applicable law and regulatory requirements.

SGI

The ability of SGI to declare and pay a dividend to shareholders is governed by applicable New York law, including the NYIL. Under Section 4105 of the NYIL, SGI is permitted to pay dividends to shareholders in any 12-month period, without the prior approval of the NYDFS in an amount equal to the lesser of 10% of its policyholders' surplus as of last financial statement filed with the NYDFS (annual or quarterly) or their adjusted net investment income for the 12-month period, as determined in accordance with Statutory Accounting Practices prescribed or permitted by the NYDFS. The NYIL also provides that SGI may distribute dividends to shareholders in excess of the aforementioned amount only upon approval thereof by the NYDFS. Even if these tests are satisfied, NYIL provides a further test in that SGI may not declare or distribute any dividends to shareholders except out of "earned surplus" (an amount equal to "unassigned funds (surplus)" as shown on SGI's statutory balance sheet, which as of March 31, 2019 and December 31, 2018 was \$481.2 million and \$475.0 million, less its "unrealized appreciation of assets"). As of March 31, 2019, SGI's unrealized appreciation of assets was \$14.3 million. The NYDFS may disapprove such dividends to shareholders if it finds that SGI will retain insufficient surplus to support its obligations and writings.

On April 30, 2019, the Company paid its surplus notes in full. Following payment in full, the following restrictions in its master transaction agreement with certain of its financial counterparties to CDS contracts insured by the Company's financial guaranty insurance policies and certain related transactions (referred to collectively as the "2009 MTA") no longer apply: the Company may not (i) make any distribution, pay, redeem, repurchase, retire, exchange or otherwise acquire its surplus notes, except on a pro rata basis and on the same terms; (ii) merge, consolidate or sell, assign, transfer or dispose of all or any material portion of its assets; (iii) pay any dividend, repurchase, redeem, exchange or convert any of its equity securities (or of any of its direct or indirect parent); (iv) issue any surplus notes; or (v) incur any indebtedness. Accordingly, the restrictive covenants in the 2009 MTA are no longer operative.

Among other requirements, Article 69 of the NYIL provides that financial guarantee insurance companies maintain minimum policyholders' surplus of \$66 million. In accordance with accounting practices prescribed or permitted by the NYDFS, as of March 31, 2019 and December 31, 2018, SGI reported policyholders' surplus of \$631.3 million and \$811.0 million, respectively. For the three months ended March 31, 2019 and 2018, SGI reported net (loss) income of \$(1.7) million and \$47.0 million, respectively.

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SGI Statutory Insurance Regulatory Requirements

SGI prepares its statutory basis financial statements in accordance with accounting practices prescribed or permitted by the NYDFS. The NYDFS recognizes only statutory accounting practices prescribed or permitted by the State of New York for determining and reporting the financial condition and results of operations of an insurance company and for determining its solvency under insurance law. The National Association of Insurance Commissioners (“NAIC”) Accounting Practices and Procedures manual (“NAIC SAP”), has been adopted as a component of prescribed or permitted practices by the State of New York. The state has adopted certain prescribed accounting practices that differ with those found in NAIC SAP. The NYDFS has the right to permit other specific practices which deviate from prescribed practices.

Set forth below are reconciliations of the net income (loss) and capital and surplus (deficit) of SGI reported in accordance with NAIC SAP to such amounts prepared in accordance with statutory accounting practices prescribed or permitted by the NYDFS for the three months ended March 31, 2019 and 2018 and as of March 31, 2019 and December 31, 2018.

(U.S. dollars in thousands)

Description	Net Income (Loss)		Capital and Surplus	
	2019	2018	2019	2018
NAIC SAP Basis	\$ 17,009	\$ 1,385	\$ (445,253)	\$ (284,236)
Effect of NY prescribed practices				
(a)	-	-	-	-
Effect of NY permitted practices				
(b)	-	-	921,561	921,561
(c)	(18,749)	45,634	154,956	173,705
(d)	-	-	-	-
(e)	-	-	-	-
(f)	-	-	-	-
NY Basis	\$ (1,740)	\$ 47,019	\$ 631,264	\$ 811,030

Permitted or Prescribed Practices

- (a) Pursuant to certain prescribed accounting practices under Articles 14 and 69 of the NYIL that differ with those found in NAIC SAP, the admissible carrying value of a share of an insurer is limited to a stipulated percentage of policyholders’ surplus, and investments in certain securities (including the Uninsured Cash Flow Certificates) are also subject to limitations. In connection with the 2009 MTA, the NYDFS permitted the Company to admit these assets notwithstanding the otherwise applicable limitations, which resulted in no difference between NAIC SAP and NY basis.
- (b) In connection with the reinsurance agreement with Assured, which closed on June 1, 2018, the NYDFS permitted the Company to set a fixed contingency reserve balance of \$5 million. This fixed reserve balance will not increase through accretion nor decrease through releases. Pursuant to prior approvals granted by the NYDFS in accordance with section 6903 of the NYIL, as of March 31, 2019 and December 31, 2018, SGI has de-recognized \$921.6 million and \$921.6 million, respectively, in the aggregate, of contingency reserves on terminated policies, and policies on which the Company has established case reserves, whereas under NAIC SAP the Company would still be required to carry such reserves. The Company applied the permitted practice described above to release contingency reserves on an obligation by obligation basis under policies insuring multiple obligations rather than on a policy by policy basis. In addition to the foregoing, the Company released contingency reserves based on a methodology pursuant to a permitted practice granted by the NYDFS.
- (c) The NYDFS granted SGI a permitted practice to de-recognize reserves for unpaid losses, unearned premium reserve and contingency reserves relating to, and expense payments (which are reflected in “Net losses and loss adjustment expenses” on the Statements of Operations and Changes in Capital and Surplus (“Statements of Operations”)) made to effect, certain transactions executed in connection with its continued remediation efforts which effectively defeased or, in-substance, commuted, in whole or in part, the policies relating thereto, whereas under NAIC SAP such reserves would continue to be carried until such time the underlying contracts were legally extinguished and the payments made to effect the transactions would have resulted in the recording of an asset, as such payments were made in exchange for the assignment to the Company or an affiliate of the Company of all rights under the aforementioned policies. As of March 31, 2019, such de-recognized reserves for unpaid losses, unearned premium reserve and contingency reserves (as of the date of the effective defeasance or, in-substance commutations) aggregated \$6.3 billion, \$17.4 million and \$4.9 million, respectively. As of December 31, 2018, such de-recognized reserves for unpaid losses, unearned premium reserve and contingency reserves (as of the date of the effective defeasance or, in-substance commutations) aggregated \$6.3 billion, \$17.4 million and \$4.9 million, respectively. As of December 31, 2015, the Company no longer sought approval for the de-recognition of unpaid losses, unearned premium reserves and contingency reserves relating to, and expense payments made which effectively defeased or, in-substance, commuted certain CDS contracts executed in connection with the consummation of the 2009 MTA and that were previously disclosed on an aggregate basis. As such CDS contracts were legally extinguished as of December 31, 2015, the associated reserves were released under NAIC SAP resulting in no difference between NAIC SAP and NY basis, and therefore the permitted practice is no longer required.
- (d) The NYDFS granted the Company a permitted practice to value the surplus notes issued by the Company in settlement of certain policy obligations in connection with the 2009 MTA at original face value of \$625.0 million in the aggregate, as compared to the estimated fair value thereof, that the Company would otherwise have been required to reflect such surplus notes in accordance with NAIC SAP. Any adjustment to the carrying value of surplus notes would result in an equal and offsetting adjustment to unassigned funds. As both surplus notes and unassigned funds are elements of policyholders’ surplus, a change in the value of the surplus notes would not affect policyholders’ surplus.
- (e) The NYDFS previously granted the Company a permitted practice to account for its ownership of the common stock of American Roads entities and Pike Pointe Holdings, LLC as salvage recoverable, which is deducted from the liability for unpaid claims or losses, whereas under NAIC SAP, the Company would

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be required to record its 100% equity ownership of these entities using GAAP equity values. As of December 31, 2018, the Company no longer applies such permitted practice.

- (f) In connection with the Restructuring Transactions (as defined in Note 3) completed on August 12, 2016, the NYDFS granted the Company permission to increase its earned surplus to the greatest extent possible given its current gross paid in and contributed surplus by allocating the entire balance of that account to earned surplus. As both earned surplus and gross paid in and contributed surplus are elements of policyholders' surplus, this permitted practice has no effect on total policyholders' surplus.

14. Assets on Deposit to Collateralize Certain of the Company's Contractual Obligations

As of March 31, 2019 and December 31, 2018, the Company had, in the aggregate, approximately \$29.3 million and \$29.9 million, respectively, on deposit to collateralize its contractual obligations under certain agreements, including reinsurance, lease and letter of credit agreements. Of such deposits, \$24.7 million and \$22.3 million and \$4.6 million and \$7.6 million are recorded on the accompanying consolidated balance sheet in "Other assets" and "Debt securities, available for sale, at fair value", respectively. In connection with the reinsurance agreement with Assured, the Company agreed to maintain \$15.6 million on deposit through June 1, 2023. In addition, debt securities with an amortized cost and fair value of \$5.7 million and \$5.9 million at March 31, 2019 and \$5.5 million and \$5.6 million at December 31, 2018, respectively, were on deposit with various regulatory authorities as required by insurance laws.

15. Financial Information of Syncora Holdings (Parent Company Only)

The condensed balance sheets, statements of operations and shareholders' equity, and statements of cash flows of Syncora Holdings as of March 31, 2019 and December 31, 2018 and for the three months ended March 31, 2019 and 2018 are set forth below:

(U.S. dollars in thousands)	2019	2018
Assets		
Debt securities available for sale, at fair value (amortized cost: \$3,346 and \$4,026).....	\$ 3,448	\$ 4,118
Cash and cash equivalents.....	1,503	908
Accrued investment income.....	27	17
Investment in subsidiaries on an equity basis:		
Syncora Guarantee Inc.....	617,698	608,948
Other subsidiaries.....	19,854	19,754
Other assets.....	923	467
Total assets.....	\$ 643,453	\$ 634,212
Liabilities and Shareholders' Equity		
Liabilities— accounts payable, accrued expenses, and other liabilities	\$ 3,352	\$ 388
Shareholders' equity		
Common shares and additional paid-in capital.....	2,718,162	2,717,633
Accumulated deficit.....	(2,089,896)	(2,085,637)
Accumulated other comprehensive income.....	11,835	1,828
Total shareholders' equity.....	640,101	633,824
Total liabilities and shareholders' equity.....	\$ 643,453	\$ 634,212

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(U.S. dollars in thousands)	<u>2019</u>	<u>2018</u>
Revenues		
Net investment income.....	\$ 26	\$ 22
Total revenues.....	<u>26</u>	<u>22</u>
Operating expenses	3,138	491
Loss before equity in net loss of subsidiaries	<u>(3,112)</u>	<u>(469)</u>
Equity in net income (loss) of Syncora Guarantee Inc.	56,055	(8,352)
Equity in net income of other subsidiaries	98	44
Equity in net income (loss) of subsidiaries	<u>56,153</u>	<u>(8,308)</u>
Net income (loss) attributable to Syncora Holdings Ltd.	<u>53,041</u>	<u>(8,777)</u>
Other comprehensive income (loss):		
Net unrealized gains (losses) on investments	12	(10)
Equity in other comprehensive income (loss) of Syncora Guarantee Inc....	9,995	(13,061)
Other comprehensive income (loss)	<u>10,007</u>	<u>(13,071)</u>
Comprehensive income (loss)	<u>63,048</u>	<u>(21,848)</u>
Change in common shares and additional paid-in-capital	529	545
Purchase of Series B preferred shares.....	(57,300)	-
Change in shareholders' equity	<u>6,277</u>	<u>(21,303)</u>
Total shareholders' equity- beginning of period	633,824	685,959
Total shareholders' equity- end of period	<u>\$ 640,101</u>	<u>\$ 664,656</u>
	<u>2019</u>	<u>2018</u>
Cash flows from operating activities:		
Operating expenses paid.....	\$ (3,036)	\$ (539)
Investment income collected.....	10	11
Other cash receipts.....	2,160	98
Net cash used in operating activities	<u>(866)</u>	<u>(430)</u>
Cash flows from investing activities:		
Proceeds from sale of debt securities	497	929
Proceeds from maturity of debt securities	1,209	12
Purchases of debt securities.....	(245)	(244)
Net cash provided by investing activities	<u>1,461</u>	<u>697</u>
Increase in cash and cash equivalents	595	267
Cash and cash equivalents—beginning of period	908	1,312
Cash and cash equivalents—end of period	<u>\$ 1,503</u>	<u>\$ 1,579</u>

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16. Discontinued Operations of American Roads LLC

On July 16, 2018, the Company announced that Pike Pointe closed the sale of American Roads LLC to American Roads AcquireCo LLC, a wholly owned subsidiary of DIF Infrastructure V for net cash proceeds of approximately \$220 million, before payment of related expenses, with provisions that provide for payment of additional amounts if specified conditions are met within 12 months of the date of the agreement. American Roads is involved in the following operations: management and operational rights to the Detroit Windsor Tunnel (“DWT”), owner and operator of four toll bridges in Alabama (between the mainland and resort communities of Orange Beach and Gulf Shores, between Montgomery and Elmore Counties, between towns in Elmore and Autauga Counties, and on a portion of the western bypass of Tuscaloosa), and the development of tolling and transportation software and technology for third parties.

On August 8, 2017, management, with Board of Directors approval, committed to a formal plan to sell American Roads LLC. Since the accounting criteria for discontinued operations were met on August 8, 2017, the Company has reflected this classification in the accompanying consolidated financial statements through July 16, 2018 (sale date of American Roads LLC). The consolidated statement of operations and comprehensive income for the three months ended March 31, 2018 presents the total revenues and total expenses of American Roads LLC in the line item “Income from discontinued operations”. The consolidated statement of cash flows for the three months ended March 31, 2018 presents the cash flows of American Roads LLC in the line items “net cash provided by (used in) operating and investing activities from discontinued operations”, respectively.

The following table summarizes the components of Income from discontinued operations for American Roads LLC for the three months ended March 31, 2019 and 2018.

(U.S. dollars in thousands)	<u>2019</u>	<u>2018</u>
Revenues		
Toll revenue.....	\$ -	\$ 6,123
Net investment income.....	-	26
Fees and other income.....	-	924
Total revenues.....	<u>-</u>	<u>7,073</u>
Expenses		
Foreign currency exchange gain.....	-	(79)
Gain on pension and other post-retirement benefits settlement.....	-	(4,099)
Operating expenses.....	-	4,385
Total expenses.....	<u>-</u>	<u>207</u>
Income from discontinued operations before income tax expense.....	-	6,866
Income tax expense.....	-	-
Income from discontinued operations, net of tax.....	<u>-</u>	<u>6,866</u>
Other comprehensive loss from discontinued operations.....	-	(3)
Comprehensive income from discontinued operations.....	<u>\$ -</u>	<u>\$ 6,863</u>

The income from discontinued operations does not include any income taxes since American Roads LLC is not a tax paying entity and is part of a consolidated U.S. federal tax return with Syncora Holdings U.S. Inc.

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The following table summarizes the components of cash flow information for American Roads LLC for the three months ended March 31, 2019 and 2018.

(U.S. dollars in thousands)	2019	2018
Cash flows from operating activities:		
Tolls collected.....	\$ -	\$ 6,330
Management fees received.....	-	108
Other operating cash receipts.....	-	857
Cash paid for operating expenses.....	-	(7,866)
Interest and dividend income collected.....	-	32
Net cash used in operating activities of discontinued operations	-	(539)
Cash flows from investing activities:		
Proceeds from sale of investments.....	-	198
Purchases of investments.....	-	(188)
Purchases of property and equipment	-	(193)
Net cash used in investing activities of discontinued operations.....	-	(183)
Decrease in cash and cash equivalents and restricted cash.....	-	(722)
Cash and cash equivalents and restricted cash- beginning of period.....	-	36,846
Cash and cash equivalents and restricted cash - end of period.....	\$ -	\$ 36,124
Summary of cash and cash equivalents and restricted cash- end of period:		
Cash and cash equivalents.....	\$ -	\$ 35,935
Restricted cash	-	189
Cash and cash equivalents and restricted cash – end of period.....	\$ -	\$ 36,124

17. Subsequent Events

On April 30, 2019, the Company paid off in full the remaining principal and accrued interest on its surplus notes. In connection with the payment in full of the Company's surplus notes, the Company received consent from more than 60% of the surplus noteholders to delete the remaining restrictive covenants of the 2009 MTA. See Note 13 for further discussion.

The Company has evaluated all subsequent events through May 13, 2019, the date the consolidated financial statements were available to be issued.